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IN THE

Supreme Court of the United States

JERRY SUMMERS, GEORGE T. LENORMAND, JEFFERY D. CRITES, LOUISE VAN RAENSBURG and JAMES E. SHAMBO, individually and on behalf of all others similarly situated,

Petitioners,

v.

STATE STREET BANK & TRUST COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. What is the proper standard for determining whether a fiduciary of an employee stock ownership plan ("ESOP") subject to the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. §§ 1001, *et. seq.*, breached its fiduciary duty of prudence by failing to diversify that ESOP's investment in employer stock before that stock lost all or most of its value?

2. Is the applicable standard different when the fiduciary is a "directed trustee" within the meaning of 29 U.S.C. § 1103(a)(1)?

PARTIES TO THE PROCEEDING

In addition to the parties identified in the caption, the following are parties to the case (and are all defendants who have previously settled all claims against them): UAL Corporation ESOP Committee, Marty Torres, Barry Wilson, Doug Walsh, Ira Levy, Don Clements, and Craig Musa.

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Petitioner respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS AND JUDGMENTS BELOW

The opinion of the Seventh Circuit (Pet. App. A) is reported at 453 F.3d 404 (7th Cir. 2006). The opinion of the district court (Pet. App. B) is not reported but may be found at 2005 U.S. Dist. Lexis 23918 (N.D. Ill. Oct. 12, 2005).

JURISDICTION

The opinion and judgment of the Court of Appeals was issued on June 28, 2006. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTES AND ADVISORY BULLETIN INVOLVED

Statutes at issue in this case include the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§ 1103, 1104, 1105, 1109, 1132 (Pet. App. C, D, E, F, and G). Also at issue is Department of Labor, Field Advisory Bulletin 2004-03 (Pet. App. H).

STATEMENT OF THE CASE

This case is a class action brought on behalf of thousands of individuals who were participants in the United Airlines Corporation Employee Stock Ownership Plan ("United ESOP" or "the Plan") during the period from November 17, 2001, through June 30, 2003.[1] In this case, Petitioners/ Plaintiffs allege that the fiduciaries of the United ESOP, including State Street Bank & Trust Company ("State Street"), breached their fiduciary duties to the Plan and its

1. R.Doc.# 178, Plfs' Add'l Facts, ¶ 1, and Exs. A-E (Class Representative Declarations) attached thereto, Appellants' App., Tab B.

participants by failing to diversify the Plan's investment in the stock of United Airlines ("United," or "UAL") even though State Street knew that United faced extreme financial problems and a significant risk of bankruptcy. Despite unmistakably clear and unusually candid warnings from United's CEO on October 17, 2001, and repeated warnings about the company's viability over the next 10 months, the Plan's fiduciaries took no action to diversify the Plan's investments. Even after State Street concluded that there was a "high risk" that UAL would not qualify for the government loan guarantees that the Company needed to survive, State Street continued to do nothing to protect the Plan and its participants from UAL's plunge into bankruptcy that essentially wiped out the Plan's assets.

The United ESOP was an employee stock ownership plan, or "ESOP", maintained pursuant to the Employee Retirement Income Security Act of 1974 (ERISA), and was "designed to invest exclusively in shares of [United's] stock."[2] Participants in the United ESOP were prohibited from diversifying their accounts under the Plan except upon a termination of employment or the satisfaction of certain age and length-of-participation requirements.[3] Instead, the direction of the United ESOP's investments was overseen by the Plan's fiduciaries: the ESOP Committee, which was the Plan's named fiduciary,[4] and State Street, which was the

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2. R.Doc.# 178, Plfs' Add'l Facts, ¶ 17 and R.Doc.# 184, Plfs' Ex. 39.

3. R.Doc.# 178, Plfs' Add'l Facts, ¶ 12 and R.Doc.# 184, Plfs' Ex. 39.

4. R.Doc.# 178, Plfs' Add'l Facts, ¶ 2 and R.Doc.# 184, Plfs' Ex. 39.

trustee for the Plan throughout the relevant time period.[5] With respect to these fiduciaries, the Plan provided that "every individual who is a fiduciary with respect to the Plan shall exercise his responsibilities with respect to the Plan in a manner consistent with ERISA and other applicable laws."[6] Similarly, the Trust Agreement provided that "the Trustee shall not be obligated to follow the direction of a named fiduciary unless such direction is ... proper within the meaning of Section 403(a) of ERISA and is not contrary to ERISA."[7]

Despite holding those fiduciary duties under the Plan and the Trust Agreement, State Street did not begin diversifying the United ESOP's investment in United stock until September 27, 2002,[8] on the eve of United's bankruptcy. However, it had been well-known to State Street for at least a year prior to that date that United was in serious financial trouble. In early 2001, it was already apparent that United was facing difficult financial prospects in the year ahead. United stated in its Form 10-K for 2000 that the "Outlook for 2001" was poor due to a decrease in business travel, rising fuel costs and other factors.[9] The prediction was accurate. In the first six months of 2001, United reported operational losses of $860 million, compared with earnings of $858

5. R.Doc.# 178, Plfs' Add'l Facts, ¶ 4 and R.Doc.# 184, Plfs' Ex. 21.

6. R.Doc.# 178, Plfs' Add'l Facts, ¶ 18 and R.Doc.# 184, Plfs' Ex. 39.

7. R.Doc.# 178, Plfs' Add'l Facts, ¶ 20 and R.Doc.# 184, Plfs' Ex. 21 at § 3.8.

8. R.Doc.# 178, Plfs' Add'l Facts, ¶¶ 171-72 and R.Doc.# 184, Plfs' Ex. 25 at UAL-SUM 00123-24.

9. R.Doc.# 178, Plfs' Add'l Facts, ¶ 38 and R.Doc.# 184, Plfs' Ex. 46.

million in the first six months of 2000.[10] On July 19, 2001, United stock closed at $34.42.[11] On September 10, 2001, United stock closed at $30.82.

United stock was thus already losing its luster when the catastrophic events of September 11, 2001, occurred, shaking the American economy and hitting the airline industry particularly hard. When the stock market re-opened on September 17, 2001, United stock closed at $17.50.[12] By September 20, 2001, Bloomberg News carried reports that United and other airlines were "seeking $17.5 billion of government aid to stave off bankruptcy."[13]

However, the clearest sign of where United was headed came on October 17, 2001, when United's CEO, Jim Goodwin, wrote an extraordinary letter to all United employees, a copy of which was filed with the SEC as an 8-K. According to that letter:

> Prior to Sept. 11, all of the major U.S. airlines were having financial difficulties as a result of the weakening economy. The economic pain was worse for us because we rely more heavily on frequent business travelers for our business than they do. . . .
>
> Then came Sept. 11.

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10. R.Doc.# 178, Plfs' Add'l Facts, ¶ 42 and R.Doc.# 184, Plfs' Ex. 40 (10-Q for 2Q 2001).

11. R.Doc.# 178, Plfs' Add'l Facts, ¶ 40 and R.Doc.# 184, Plfs' Ex. 50.

12. R.Doc.# 178, Plfs' Add'l Facts, ¶ 44 and R.Doc.# 184, Plfs' Ex. 50.

13. R.Doc.# 178, Plfs' Add'l Facts, ¶ 46 and R.Doc.# 184, Plfs' Ex. 51.

> In the wake of that day's horrific events, we are in nothing less than a fight for our life. Never in our 75-year history have we faced an economic challenge of this magnitude, where the drop-off in air travel has been so unexpected and prolonged.
>
> Our number one priority now is to get United into a financial position that will allow us to continue operating. We are not there yet. To get there, we must focus on breakeven cash flow. That means being in the position where we have as much money coming into our bank account as we have streaming out of it. In the past, we struggled to make a profit. Now we're in a struggle just to survive.
>
> * * *
>
> Let me illustrate the financial hole we're in. Before Sept. 11th, we were not in a comfortable financial state, with costs exceeding our revenue on a daily basis. Today, the situation is exacerbated with costs exceeding revenue at four times the pre-Sept. 11 rate. Today, we are literally hemorrhaging money.
>
> Clearly, this bleeding has to be stopped – and soon – or United will perish sometime next year. . . .[14]

At the time of the letter, United was burning cash at a rate of $15 million per day.[15] The company had lost $1.6

14. R.Doc.# 178, Plfs' Add'l Facts, ¶ 47 and R.Doc.# 184, Plfs' Ex. 32, Appellants' App., Tab D.

15. R.Doc.# 178, Plfs' Add'l Facts, ¶ 61 and R.Doc.# 184, Plfs' Ex. 41 at P 0050.

billion for the three-month period ending September 30, 2001, and $2.2 billion for the nine month period ending that same date.[16] On the two market days following the release of the Goodwin letter, United stock dropped more than 20%, closing at $15.05 on October 18, 2001.[17]

Goodwin resigned on October 28, 2001, but the prospects for the company remained dire. The Buckingham Research Group ("Buckingham") stated the resignation "will probably not stave off the inevitable. After hitting new lows last week, we believe that UAL's share price is starting to reflect a possible Chapter 11 filing." The Buckingham report noted that employees "do not want to grant concessions," yet "[w]ithout those concessions there is no way this company can survive."[18]

The warnings about United's likely bankruptcy were numerous and dire, and they continued for the next several months. The public information included the following:

> November 2, 2001: Solomon Smith Barney reports that labor costs and work rules were "UAL's Achilles heel," and that "reorganization risk is material."[19]
>
> November 12, 2001: *Business Week* states that "[i]f UAL continues to bleed red ink, some

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16. R.Doc.# 178, Plfs' Add'l Facts, ¶ 57 and R.Doc.# 184, Plfs' Ex. 41 at P 0042-44.

17. R.Doc.# 178, Plfs' Add'l Facts, ¶ 48 and R.Doc.# 184, Plfs' Ex. 50.

18. R.Doc.# 178, Plfs' Add'l Facts, ¶ 53 and R.Doc.# 184, Plfs' Ex. 61.

19. R.Doc.# 178, Plfs' Add'l Facts, ¶ 54 and R.Doc.# 184, Plfs' Ex. 59.

analysts say bankruptcy – which would allow it to abrogate its union contracts – may be its only hope."[20]

January 2002: Moody's Investor Services downgrades United's unsecured debt ratings to Caa2, reflecting its "view that United's cash flow has deteriorated and that large cash losses from operations in the last few months have eroded UAL's financial profile." Moody's further notes that "the company's high cost base will hamper recovery of adequate cash levels."[21]

January 23, 2002: A Buckingham report states, "We believe that the survivability of this airline in its current form is in doubt."[22]

February 1, 2002: *The New York Times* reports that "Several industry experts and two senior executives at rival airlines said they were beginning to conclude that United ... would have no choice but to file for Chapter 11 bankruptcy protection later this year if it were to have any hope of turning itself around."[23]

February 6, 2002: Morgan Stanley reports: "As most observers of the airline industry know by

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20. R.Doc.# 178, Plfs' Add'l Facts, ¶ 62 and R.Doc.# 184, Plfs' Ex. 52.

21. R.Doc.# 178, Plfs' Add'l Facts, ¶ 117 and R.Doc.# 184, Plfs' Ex. 26 at SSB 00850 (State Street "Watchlist Committee" report dated Jan. 18, 2002).

22. R.Doc.# 178, Plfs' Add'l Facts, ¶ 73 and R.Doc.# 184, Plfs' Ex. 63.

23. R.Doc.# 178, Plfs' Add'l Facts, ¶ 75 and R.Doc.# 184, Plfs' Ex. 54.

now, no carrier that loses the kind of money UAL did in 2001 ($1.8 billion) has ever turned itself around without seeking protection in chapter eleven."[24]

April 2002: United reports first quarter operational losses of $711 million, compared with $391 million in losses in the first quarter of 2001.[25]

May 2002: J.P. Morgan reports: "The market appears to be treating UAL as terminally ill."[26]

June 24, 2002: United's CEO, Jack Creighton, states: "We're now burdened by short-term financing needs that are driven by the aftermath of September 11 and aggravated by the weak economic recovery. While we continue to explore financing alternatives, we don't believe they will be sufficient because our access to the capital markets has been severely restricted."[27]

June 24, 2002: United files for federal loan guarantees, four days before the deadline for doing so.[28] However, the guidelines for such guarantees

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24. R.Doc.# 178, Plfs' Add'l Facts, ¶ 76 and R.Doc.# 184, Plfs' Ex. 64 at SSB 00535.

25. R.Doc.# 178, Plfs' Add'l Facts, ¶ 81 and R.Doc.# 184, Plfs' Ex. 43 at P 0143 (10-Q for 1Q 2002).

26. R.Doc.# 178, Plfs' Add'l Facts, ¶ 86 and R.Doc.# 184, Plfs' Ex. 66 at SSB 00598.

27. R.Doc.# 178, Plfs' Add'l Facts, ¶ 88 and R.Doc.# 184, Plfs' Ex. 37 at UAL-SUM 002138.

28. R.Doc.# 158, Plaintiffs' Response to Defendant State Street Bank & Trust Company's Statement of Facts ("Plfs' Response") at 4-5.

> require that the air carrier demonstrate that it has a "financially sound" business plan and that its creditors, including employees, will make concessions "that will improve the financial condition of the air carrier. . . ." 14 C.F.R. §§ 1300.17(b)(4)(i), (v).
>
> August 14, 2002: UAL announces that, without ATSB loan guarantees, it might have to file for bankruptcy in the fall, and that it would have to obtain concessions from the unions in order to get the loan guarantees.[29]

This situation was well-known to Respondent State Street. In 2001, on its own initiative, State Street monitored United stock through its agent, CitiStreet,[30] and on December 20, 2001, the CitiStreet Watchlist Committee placed United on its Watchlist because of the drop in stock price and the public statements made in the Goodwin letter of October 17, 2001, among other factors.[31] United remained on that Watchlist through September 2002, by monthly vote of the Watchlist Committee.[32]

On May 8, 2002, State Street went so far as to elevate United stock for internal review by its Fiduciary Committee,

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29. R.Doc.# 178, Plfs' Add'l Facts, ¶ 141 and R.Doc.# 184, Plfs' Ex. 26 at SSB 0881 (Watchlist Committee Report dated Sept. 20, 2002).

30. R.Doc.# 17, Plfs' Add'l Facts, ¶ 111 and R.Doc.# 186, Plfs' Ex. 1 (Daniels Dep.) at 17:16-20 and 66:16-20; Plfs' Ex. 2 (Driscoll Dep.) at 30:13-14.

31. R.Doc.# 178, Plfs' Add'l Facts, ¶ 113 and R.Doc.# 184, 186, Plfs' Ex. 23 at SSB 00843, Plfs' Ex. 1 (Daniels Dep.) at 24:3-18.

32. R.Doc.# 178, Plfs' Add'l Facts, ¶ 115 and R.Doc.# 184, Plfs' Ex. 26 at SSB 00848, 00857, 00861, 00865, 00869, 00873, 00877, 00881.

in accordance with its Fiduciary Charter, which provided that "[i]f continued deterioration is noted then the company may be elevated for review to the Fiduciary Committee."[33] At the same time, State Street began consulting with counsel about whether it had an obligation to override the Plan by selling United Stock,[34] and was informed that it had a duty "to disregard the terms of the plan and trust agreement if it determines that it is no longer prudent for the plan to continue to hold the UAL shares."[35]

Significantly, on May 22, 2002, a State Street internal report opines that "there is a high risk that UAL will not be able to come to terms with some of the union employees to accept wage concessions, which jeopardizes the $1.8 billion loan guarantees by the government."[36]

At the same time that State Street monitored United stock and considered its obligations to diversify the Plan's investments, State Street was also fully aware that the named fiduciaries of the ESOP Committee had never discussed United's financial condition or whether it should sell the $1 billion in United stock that the ESOP held.[37]

However, State Street did not take ***any*** action to protect the United ESOP's assets until August 15, 2002, when State

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33. R.Doc.# 178, Plfs' Add'l Facts, ¶ 127 and R.Doc.# 184, Plfs' Ex. 5 (Feely Dep.) at 25:22-26:5; Plfs' Ex. 26 at SSB 00885.

34. R.Doc.# 178, Plfs' Add'l Facts, ¶ 130 and R.Doc.# 186, Plfs' Ex. 12 (Smith Dep.) at 46:5-22, 59:1-2.

35. R.Doc.# 178, Plfs' Add'l Facts, ¶ 131 and R.Doc.# 186, Plfs' Ex. 12 (Smith Dep.) at 44:9-45:3.

36. R.Doc.# 158, Plfs' Response at 5 and R.Doc.# 130 (State Street report).

37. R.Doc.# 178, Plfs' Add'l Facts, ¶¶ 146-147 and R.Doc. # 184, Plfs' Exs. 5 and 25.

Street finally informed United that it had "put United on a 'watch list' due to the decreasing stock price and the possible bankruptcy filing."[38]

A special meeting of the ESOP Committee convened on August 20, 2002, at which time State Street first informed the other fiduciaries of the obligation to review whether it was prudent to retain United stock in the Plan.[39] At a subsequent meeting in late August, State Street was appointed as the investment manager for the United ESOP,[40] and on September 27, 2002, State Street finally began selling the Plan's shares of United stock.[41] On September 27, 2002, the stock closed at $2.36.[42]

According to Petitioners' expert, Daniel R. Fischel, had the fiduciaries commenced selling United stock within 30 days of the October 17, 2001, Goodwin letter and placed those shares in an alternative, low-risk fund, they would have saved Plan participants from approximately $540 million in losses.[43]

Plaintiffs filed suit on behalf of the United ESOP on February 28, 2003, claiming, pursuant to ERISA, 29 U.S.C.

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38. R.Doc.# 178, Plfs' Add'l Facts, ¶ 143 and R.Doc.# 184, Plfs' Ex. 25 at UAL SUM 00047.

39. R.Doc.#178, Plfs' Add'l Facts, ¶ 156 and R.Doc.# 184, Plfs' Ex. 25 at UAL-SUM 00047.

40. R.Doc.# 178, Plfs' Add'l Facts, ¶ 167 and R.Doc.# 184, Plfs' Ex. 25 at UAL-SUM 0080.

41. R.Doc.# 178, Plfs' Add'l Facts, ¶¶ 171-72 and R.Doc.# 184, Plfs' Ex. 25 at UAL-SUM 00123-24.

42. R.Doc.# 178, Plfs' Add'l Facts, ¶ 103 and R.Doc.# 184, Plfs' Ex. 50.

43. R.Doc.# 115, Supplemental Report of Daniel R. Fischel at ¶ 17(2) (attached as Ex. 1 to Declaration of Daniel R. Fischel).

§§ 1109 and 1132(a)(2), that the Plan's fiduciaries had breached their fiduciary duties by failing to diversify the ESOP's investments at an earlier time. All defendants other than State Street settled the claims against them.

On October 12, 2005, less than a week before trial, the United States District Court for the Northern District of Illinois granted summary judgment in favor of State Street, finding that it had not breached its fiduciary duty because it had no duty to sell until there was evidence of an "imminent collapse" by United, a point on which it found no genuine issues of material fact. *Summers v. UAL Corp. ESOP Comm.*, 2005 U.S. Dist. Lexis 23918, *14-15 (Pet. App. B). On June 28, 2006, the Court of Appeals for the Seventh Circuit affirmed the district court's decision. *Summers v. State Street Bank & Trust Co.*, 453 F.3d 404 (7th Cir. 2006) (Pet. App. A).

REASONS FOR GRANTING THE PETITION

The Seventh Circuit's decision in this case created a conflict among the Courts of Appeals regarding the duties of ERISA fiduciaries to diversify employer-stock investments made pursuant to ESOPs. The Seventh Circuit's new standard also conflicts with prior decisions of this Court and touches directly on an important question that is the subject of substantial ongoing litigation in the federal courts. The Court should resolve this conflict to allow that ongoing litigation to proceed in an efficient manner.

In addition, the Seventh Circuit's decision in this case exposes and contributes to a conflict among the Courts of Appeal regarding whether the duty of an ERISA fiduciary to diversify an ESOP's employer-stock investments is lessened when the fiduciary is a "directed trustee" acting pursuant to 29 U.S.C. § 1103(a)(1). Petitioners believe the Seventh Circuit came down on the correct side of this split, but

recognize that the Courts of Appeals are in conflict and that the issue of directed-trustee liability would likely need to be resolved in any opinion by this Court on the merits of this suit. In any event, a resolution of the conflict would set clear standards for ESOP fiduciaries and provide much-needed guidance to lower courts that are presently faced with numerous different opinions as to the proper standard of liability for directed trustees.

I. THE SEVENTH CIRCUIT'S STATED STANDARD FOR ASSESSING WHETHER AN ESOP FIDUCIARY BREACHED ITS DUTY TO DIVERSIFY THE ESOP'S INVESTMENT IN EMPLOYER STOCK CONFLICTS WITH DECISIONS FROM OTHER COURTS OF APPEALS AND PRIOR DECISIONS OF THIS COURT

A. The Seventh Circuit's Decision Created a Conflict on the Previously Settled Issue of a Fiduciary's Duty to Diversify

Prior to the Seventh Circuit's decision in this case, the Courts of Appeals were generally in agreement as to the proper standard for determining whether an ESOP fiduciary had breached the ERISA duty of prudence by failing to diversify an ESOP's investment in employer stock. As originally formulated in *Moench v. Robertson*, 62 F.3d 553, 571-72 (3d Cir. 1995):

> an ESOP fiduciary who invests the assets in employer stock is entitled to a presumption that it acted consistently with ERISA by virtue of that decision. However, the plaintiff may overcome that presumption by establishing that the fiduciary abused his discretion by investing in employer securities. . . . [T[he plaintiff must show that the

> ERISA fiduciary could not have believed reasonably that continued adherence to the ESOP's direction was in keeping with the settlor's expectations of how a prudent trustee would operate.

Until this case, the *Moench* standard had been recognized as the prevailing standard by every Court of Appeals that considered the issue. *See, e.g., LaLonde v. Textron, Inc.*, 369 F.3d 1, 4, 6 (1st Cir. 2004); *Kuper v. Iovenko*, 66 F.3d 1447, 1458-59 (6th Cir. 1995); *Wright v. Oregon Metallurgical*, 360 F.3d 1090, 1098-98 (9th Cir. 2004) (questioning *Moench* standard but applying it). *See also, e.g., In re Polaroid ERISA Litig.*, 362 F. Supp. 2d 461, 474-75 (S.D.N.Y 2005); *Smith v. Delta Air Lines, Inc.*, 422 F. Supp. 2d 1310, 1327-31 (N.D. Ga. 2006); *In re Sprint Corp. ERISA Litig.*, 388 F. Supp. 2d 1207, 1221-23 (D. Kan. 2004). As the Sixth Circuit stated in adopting the *Moench* standard, a plaintiff can rebut the presumption "by showing that a prudent fiduciary acting under similar circumstances would have made a different investment decision." *Kuper*, 66 F.3d at 1459.

However, in the opinion below, the Seventh Circuit acknowledged *Moench* and its progeny, but adopted a new, and unworkable, standard. First, the Seventh Circuit adopted a *per se* rule that a continuous, steep, and unmitigated decline in a company's stock, coupled with evidence that the underlying company continues to hemorrhage money and fails to address the problems causing the decline, can never create a duty to diversify an ESOP's investment in company stock. Specifically, with regard to United, the court ruled that as the stock price of UAL plummeted, "at *every* point in the long slide of United's stock price, that price was the best estimate available either to State Street or to the Committee of the company's value . . . and so neither fiduciary was

required to act on the assumption that the market was overvaluing United." 453 F.3d at 408-09 (emphasis in original).

In other words, the Seventh Circuit ruled that an ESOP fiduciary should never be held to a duty of diversifying an ESOP because the company's stock value was declining and there were strong indications that it would plummet further – and the court so held without considering what those indications were in this case, and it furthermore failed to analyze the intentions of the Plan's settlor. *See id.*

No other Circuit has ever adopted such a *per se* rule, as the *Moench* standard anticipates a review of all of the relevant facts to determine whether a decline in the stock price, combined with available information about the state of the company, meant that the employer stock was no longer a prudent investment. *See Moench*, 62 F.3d at 571-72. *See also Kuper*, 66 F.3d 1447 (considering all facts and determining that plaintiff failed to satisfy burden because the price of the shares "fluctuated significantly" over the relevant time period); *Wright*, 360 F.3d at 1109 (no claim because no allegation or facts indicating that the company's viability was in question); *Lalonde*, 369 F.3d at 7 (concern over inability of company to "survive its downsizing," coupled with a failure to protect the plan's assets, is sufficient to state a claim). This is the preferred approach, as it permits and requires courts to take into consideration all of the facts surrounding the employer's stock, and the prospects for that stock, in determining whether it was a prudent investment for the ESOP in question.

Moreover, the Seventh Circuit further exacerbated this Circuit split when it also ruled that, independent of a plummeting stock price, a fiduciary may nonetheless be held liable for not taking into account the increased risk of

investing in that stock. While this basic concept does not conflict with *Moench* and its progeny, the Seventh Circuit's formulation of its standard does conflict with those decisions.

Under the Seventh Circuit's standard, a fiduciary's potential liability would be based on an ad hoc analysis of the risk borne by individual plan participants. Although the Seventh Circuit did not articulate a clear test, the contemplated analysis has two steps: (1) an assessment of whether risk to the owners of the stock had increased significantly, *see* 453 F.3d at 408-09, and (2) a ***participant-by-participant*** analysis of whether an ESOP participant's other sources of income or retirement savings allowed that participant to absorb the increased risk in the ESOP investment. *See id.* at 409-11.

It is in the second step of this analysis that the Seventh Circuit again departed from the opinions of its sister Circuits. The court indicated that the liability consideration must take into account "the employee-shareholders' total wealth," including their ESOP holdings, "their expected earnings and fringe benefits as employees of United," and the likelihood that the increased risk in United's stock price jeopardized the employees' future employment. *Id.* at 409. As the court further elaborated:

> The tension between the goal of protection against risk and the goal of a portfolio dominated by a single stock is not acute if the participants in the ESOP have adequate sources of income or wealth that are not correlated with the risk of that stock, so that the ESOP is not their primary financial asset. But if they don't have substantial other wealth the goals cannot be reconciled, though they can be compromised by requiring fiduciaries to begin diversifying the ESOP's assets at the point

> at which an increase in the riskiness of the assets . . . would have induced the creators of the ESOP either to have not created it at all or to have required at least partial diversification.

Id. at 410.

Thus, the Seventh Circuit would rest fiduciary liability for failure to diversify an ESOP's investments on a consideration of each plan participant's assets and projected wealth ***outside of the ESOP***. Accordingly, with respect to any plan participant who had significant non-ESOP assets, there would apparently never be any fiduciary duty to diversify that participant's ESOP account – even if the risk in owning Company stock had increased so substantially that the ESOP's creators would not have wished the trustees to retain the stock. The Seventh Circuit's opinion thereby gives rise to the inevitable circumstance in which a fiduciary could be held not liable for failing to diversify the ESOP investments as to one well-heeled participant but liable for failing to diversify the same investment in the same plan for a participant with fewer assets outside of the ESOP.

The conflict between such a standard and the standard adopted by other Circuits is clear. Under *Moench*, the focus of the standard is whether a plaintiff can prove that the state of employer stock had deteriorated to such a degree that it was an abuse of discretion to continue to hold those shares, given the settlor's intent in creating the ESOP. *See* 62 F.3d at 553. The focus is directly, and correctly, on the plan's investment and whether that investment is no longer in accord with the purposes of the ESOP. A fiduciary is either liable to the plan as a whole, or is not. *See also Kuper*, *supra*, 66 F.3d at 1458-60 (focus on prudence of investment of plan assets as a whole); *Lalonde*, *supra*, 369 F.3d at 6-7 (same); *Wright*, *supra*, 360 F.3d at 1098-99 (same).

Moreover, the Seventh Circuit's standard would be impossible to administer. It is unlikely that in actual application of the standard, any court (or any fiduciary attempting to fulfill its duties to a plan) would be able to determine precisely the point at which a particular participant could be deemed as having sufficient outside income or savings that would buffer that participant against the increased risk of an ESOP investment. Any distinction between an individual deemed able to absorb the increased risk and an individual not able to do so would necessarily be arbitrary and would apparently not take into consideration whether the participant *wanted* to carry that additional risk. And perhaps most importantly, that distinction is completely divorced from what should be the key considerations in assessing fiduciary liability: the nature of the investment, the deterioration of that investment, the effect of that deterioration on the ESOP and its relation to the settlor's intent, and the fiduciary's actions or failure to act. The Seventh Circuit's standard is unworkable and in conflict with decisions of the other Circuits. This Court should grant certiorari to resolve that conflict.

B. By Looking to Participants' Assets Outside of the ESOP Trust, The Seventh Circuit's Standard Also Conflicts With Established Law of This Court and the Courts of Appeals Regarding Plan-Wide Relief and Uniform Treatment of Plan Participants

The Seventh Circuit's standard, by looking to assets and holdings of particular participants outside the plan, and by thereby requiring different treatment of similarly situated plan participants, also clearly conflicts with decisions from this Court and the Courts of Appeals which require suits for mismanagement of plan assets to seek plan-wide relief and require fiduciaries to treat similarly situated participants in a uniform fashion.

It has been well-established law for more than 20 years that suits concerning breaches of fiduciary duty brought pursuant to 29 U.S.C. §§ 1109(a) and 1132(a)(2) must be brought on behalf of "the plan as a whole." *Massachusetts Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 139, 105 S. Ct. 3085, 87 L. Ed. 2d 96 (1985). As the Court stated, "the entire text [of the statute] persuades us that Congress did not intend . . . to authorize any relief except for the plan itself," and thus suits for individual damages are not permitted under ERISA. *Id.* at 144.[44]

Over the years, the Courts of Appeals have uniformly followed this standard, and required that all suits for breaches of fiduciary duty brought pursuant to 29 U.S.C. §§ 1109(a) and 1132(a)(2) must be brought on behalf of a plan, to the exclusion of suits brought by participants to recover individual damages. *See, e.g., Dobson v. Hartford Fin. Servs. Group, Inc.*, 389 F.3d 386, 397-98 (2d Cir. 2004); *In re Schering-Plough Corp. ERISA Litig.*, 420 F.3d 231, 238-41 (3d Cir. 2005); *LaRue v. DeWolff, Boberg, & Assocs.*, 450 F.3d 570, 573-74 (4th Cir. 2006); *Kuper v. Iovenko*, 66 F.3d 1447, 1452-53 (6th Cir. 1995); *Magin v. Monsanto Co.*, 420 F.3d 679, 687-88 (7th Cir. 2005); *Farr v. US West, Inc.*, 58 F.3d 1361, 1364 (9th Cir. 1995).

The Seventh Circuit's decision in this case is contrary to that rule. The inevitable outcome of that court's new

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44. Subsequent to *Russell*, this Court ruled in *Varity Corp. v. Howe*, 516 U.S. 489, 511-15, 116 S. Ct. 1065, 134 L. Ed. 2d 130 (1996), that individual suits for breaches of fiduciary duty are permissible under § 1132(a)(3) in circumstances where the claims are not covered by 29 U.S.C. § 1109(a), which concerns fiduciary management of plan assets. *Varity* does not apply to suits such as this, which concern the management of plan assets, and are thus subject to § 1109(a) and must be brought pursuant to § 1132(a)(2).

standard will be that some participants will have a claim under § 1109(a) for a fiduciary's failure to diversify an ESOP's investments, while other participants in that same plan will not. *See* 453 F.3d at 410. The Seventh Circuit would apparently require or endorse individual suits for damages under §§ 1109(a) and 1132(a), since no claim for breach of fiduciary duty could be assessed on a plan-wide basis, or at least it would require awards of damages to individual participants rather than to the plan as a whole. That would be contrary to the language and purposes of the statue as construed by this Court in *Russell.*

Similarly, the Seventh Circuit's proposed standard runs counter to the well-established, and common-sense, rule that a fiduciary must administer an ERISA plan in a consistent fashion as to plan participants in similar or identical circumstances. In numerous instances, the Courts of Appeals (including the Seventh Circuit) have ruled that where an ERISA fiduciary applies a plan provision inconsistently to similarly situated participants, those actions are evidence that the fiduciary has acted arbitrarily and capriciously, and that its decision is therefore subject to reversal. *See, e.g., Dennard v. Richards Group, Inc.*, 681 F.2d 306, 314 (5th Cir. 1982); *Russo v. Health, Welfare, & Pension Fund*, 984 F.2d 762, 766 (7th Cir. 1993); *Pilon v. Retirement Plan for Salaried Employees of Great Northern Nekoosa Corp.*, 861 F.2d 217, 219-20 (9th Cir. 1988); *Wagener v. SBC Pension Benefit Plan*, 407 F.3d 395, 404 (D.C. Cir. 2005).

Yet, under the standard outlined by the Seventh Circuit, two plan participants with precisely the same amount of employer stock in their ESOP accounts, who are thus subject to identical risks for identical amounts of money, would have to be treated differently from each other if they had significantly different assets or savings outside of their ESOP

holdings. This is yet another conflict that this Court should resolve to avoid future confusion over the applicable standards.

C. Setting a Uniform Standard Is Necessary Given the Amount of Pending Litigation Concerning These Issues

The questions presented in this petition are not simply esoteric issues limited to this case. To the contrary, the contours of the fiduciary duties owed by ESOP fiduciaries to diversify employer-stock investments is a heavily litigated area of ERISA law. One survey of the scope of such litigation found that

> [a]s of January 25, 2005, there have been approximately ***fifty*** decisions in cases that allege breach of ERISA fiduciary duty after employer stock significantly declined. The outcome of these cases varies widely.

Craig C. Martin & Elizabeth L. Fine, *ERISA Stock Drop Cases: An Evolving Standard*, 38 J. MARSHALL L. REV. 889, 901 (2005) (emphasis added).

Since then, in just 2006 to date, Petitioners are presently aware of decisions rendered in fourteen cases, aside from this case, in which the plaintiffs have alleged that an ERISA plan fiduciary breached its duty of prudence by failing to either diversify that plan's investment in employer stock or remove employer stock as an investment option. *See In re Aquila ERISA Litig.*, 2006 U.S. Dist. Lexis 49100 (W.D. Mo. July 18, 2006); *In re Merck & Co., Inc., Sec. Derivative and ERISA Litig.*, 2006 U.S. Dist. Lexis 53729 (D.N.J. July 11, 2006); *Rankin v. Rots*, 2006 U.S. Dist. Lexis 45706 (E.D. Mich. June 28, 2006); *DiFelice v. U.S. Airways, Inc.*, 436 F. Supp. 2d 756 (E.D. Va. 2006); *Edgar v. Avaya, Inc.*, 2006

U.S. Dist. Lexis 23151 (D.N.J. Apr. 24, 2006); *Smith v. Aon Corp.*, 2006 U.S. Dist. Lexis 27297 (N.D. Ill. Apr. 12, 2006); *In re GM ERISA Litig.*, 2006 U.S. Dist. Lexis 16782 (E.D. Mich. Apr. 6, 2006); *In re Cardinal Health, Inc. ERISA Litig.*, 424 F. Supp. 2d 1002 (S.D. Ohio 2006); *Smith v. Delta Airlines, Inc.*, 422 F. Supp. 2d 1310 (N.D. Ga. 2006); *In re RCN Litig.*, 2006 U.S. Dist. Lexis 12929 (D.N.J. Mar. 21, 2006); *In re Ferro Corp. ERISA Litig.*, 422 F. Supp. 2d 850 (N.D. Ohio 2006); *Rogers v. Baxter Int'l.*, 417 F. Supp. 2d 974 (N.D. Ill. 2006); *Sherrill v. Federal-Mogul Corp. Ret. Programs Comm.*, 413 F. Supp. 2d 842 (E.D. Mich. 2006); *In re Syncor ERISA Litig.*, 410 F. Supp. 2d 904 (N.D. Cal. 2006).

The issues raised in this petition for certiorari are the subject of massive ongoing litigation in the lower courts. The present split in the Circuits presents an opportunity for the Court to resolve that conflict, provide much-needed guidance to the lower courts, and promote efficient resolution of these and other cases presently pending within the federal system.

II. THE COURTS OF APPEALS ARE IN CONFLICT ABOUT THE EFFECT, IF ANY, THAT A FIDUCIARY'S STATUS AS A "DIRECTED TRUSTEE" UNDER 29 U.S.C. § 1103(a)(1) HAS ON THE DUTY TO DIVERSIFY AN ESOP'S INVESTMENT IN EMPLOYER STOCK

The Courts of Appeals are currently fractured as to how, if at all, the standard for determining when an ESOP's investments must be diversified applies when the fiduciary in question is a "directed trustee" acting pursuant to 29 U.S.C. § 1103(a)(1). In this case, the Seventh Circuit indicated that the same standard should apply to named fiduciaries (in this case, the UAL Corporation ESOP Committee) and directed

trustees (such as Respondent State Street). *See, e.g.*, 453 F.3d at 406-07. Petitioners believe the Seventh Circuit was correct on this point but misstated the applicable standard of liability, as noted above. However, Petitioners recognize that the Courts of Appeals differ on this issue and that the issue will likely have to be addressed in any opinion by this Court on the merits of this suit.

The Seventh Circuit made no distinction between the standard that applies to directed trustees and the standard that applies to named fiduciaries, although it acknowledged that other courts have found that there should be a distinction. *See id.* at 406. The court ruled that directed ESOP trustees have a duty of prudence under 29 U.S.C. § 1104(a)(1)(B), modified to reflect the fact that the duty to diversify does not generally apply to ESOP fiduciaries. *See id.*

However, the Seventh Circuit concluded that a directed ESOP trustee has a duty to reject imprudent directions from a named fiduciary because

> the directed trustee "shall be subject to the *proper* directions of [the named] fiduciary which are made in accordance with the terms of the plan and *which are not contrary to [ERISA].*" § 1103(a)(1) (emphasis added). An imprudent direction cannot be a proper direction since the trustee has an express statutory duty of prudence.

453 F.3d at 406. Thus, the court found that directed trustees therefore have a duty to "disobey the named fiduciary's directions when it is plain that they are imprudent." *Id.* at 407. Therefore, the court concluded, for a directed trustee "knowingly to invest [trust assets] imprudently or let them remain invested imprudently is irresponsible behavior for a trustee, whose fundamental duty is to take as much care with

trust assets as he would with his own property." *Id.* As a result, the Seventh Circuit formulated and applied its standard without drawing any distinction between the duties owed to an ESOP by directed trustees versus other fiduciaries. *See id.* at 407, 408, 410.

The Eighth Circuit, in one of its decisions on the issue, is largely in accord with the Seventh Circuit. In *First-Tier Bank, N.A. v. Zeller*, 16 F.3d 907, 911 (8th Cir. 1994), the court held that directed trustees are "not relieved of [their] duties to conform to the prudent man standard of care, 29 U.S.C. § 1104(a) [and] to attempt to remedy known breaches of duty by other fiduciaries. . . ."

A different decision from the Eighth Circuit and decisions by the Third and Eleventh Circuits are in conflict with the Seventh Circuit and the Eighth Circuit in *First-Tier.* In *Maniace v. Commerce Bank of Kansas City*, 40 F.3d 264, 268 (8th Cir. 1994), the court held that "[t]he obligations of a directed trustee are something less than that owed by typical fiduciaries" and concluded that the directed trustee had no "'residual' duties" that would require it to diversify the ESOP's investments. The Third and Eleventh Circuits have stated their views more concisely, albeit in *dicta* in cases that did not involve directed trustees. *See Moench*, *supra*, 62 F.3d at 571 (named "fiduciaries should not be immune from judicial inquiry, as a directed trustee essentially is"); *Herman v. NationsBank Trust Co.*, 126 F.3d 1354, 1361 (11th Cir. 1997) (a directed trustee "is not subject to the fiduciary requirement in § 1104(a) to act prudently").

Other Circuits have also touched on the issue, but have not clearly articulated applicable standards. In *Lalonde*, *supra*, 369 F.3d at 7, the First Circuit did not outline with specificity the fiduciary duties, if any, it believed an ESOP directed trustee owed to an ESOP, other than to hold that

"[i]t would subvert the purposes of ERISA to permit lawsuits against plan fiduciaries . . . every time a company's fortunes took a relatively unexceptional turn for the worse."

Similarly, in *Wright*, *supra*, 360 F.3d at 1102, the Ninth Circuit held that "directed trustees . . . cannot be held liable for following the investment instructions provided by a plan's fiduciaries." However, the court declined to reach the question of whether it would have been a breach of fiduciary duty for a directed trustee to follow instructions that it knew to be imprudent. *See id.*

To add to the considerable confusion already existing among the courts, in 2004 the Department of Labor issued a bulletin that sets forth its view on the fiduciary responsibility of a directed trustee to diversify an ESOP's investments. *See* U.S. Dept. of Labor, Field Assistance Bulletin No. 2004-03 (December 17, 2004) ("FAB No. 2004-03") (Pet. App. H). According to that bulletin, directed trustees who do not have non-public information have a duty to reject a fiduciary's direction to invest in employer stock only

> in limited, extraordinary circumstances, where there are clear and compelling public indicators . . . that call into serious question a company's viability as a going concern.

Id. at 5-6.

This standard has been at least nominally followed by several district courts. *See DiFelice v. U.S. Airways, Inc.*, 397 F. Supp. 2d 735, 751-52 (E.D. Va. 2005); *In re Worldcom, Inc., ERISA Litig.*, 354 F. Supp. 2d 423, 445-48 (S.D.N.Y. 2005); *In re RCN Litig.*, 2006 U.S. Dist. Lexis 12929, *13-16 (D.N.J. Mar. 21, 2006). The Seventh Circuit is the only Court of Appeals to address the standard set forth in FAB 2004-03. In doing so (in this case), that court concluded that

the DOL's guidance "is not an administrable standard" and that it would require diversification by a directed trustee only when it "will almost certainly be too late." 453 F.3d at 411.

The Seventh Circuit is correct on that point, and is furthermore correct that the same standard of liability should apply to all ESOP fiduciaries, whether they are directed trustees or not. ERISA expressly contemplates that directed trustees are not immune from liability if they follow instructions that are "contrary to" the statute. 29 U.S.C. § 1103(a)(1). Thus, if a named fiduciary gives an instruction to a trustee that is imprudent under ERISA, the trustee may be held liable for following that instruction – especially if, as is in this case, the trustee has reason to suspect that the instruction is imprudent.

That reading of the statute is bolstered by the fact that any fiduciary, including a directed trustee, can be held liable if he knows that another fiduciary has committed a breach but takes no action to remedy that breach. *See* 29 U.S.C. § 1105(a)(3). This basic requirement is undercut, or simply ignored, by the approach of the Third and Eleventh Circuits, which would apparently allow a directed trustee to avoid liability for failing to divest an ESOP's investments, even when it was imprudent for the named fiduciary to invest them as such. A directed trustee should be held to the same duty as a named fiduciary, or else directed trustees will avoid liability for following investment instructions that violate ERISA's standard of prudence.

Any other standard would provide a directed trustee with excessive and unwarranted protection from liability. Indeed, under even the *Moench* standard, all ESOP fiduciaries are already entitled to a ***presumption*** that an investment in employer stock is prudent. *See* 62 F.3d at 571. To provide an additional layer of protection to directed trustees for

investments in employer stock would essentially render them "immune from judicial inquiry." *See id.* That cannot, and should not, be the case where, as in this case, the trustee (1) had access to repeated public statements from the company and third-party sources that the company was at significant risk of bankruptcy, (2) knew that the risk of investing in the company had increased significantly, as demonstrated by the company's massive cash losses and inability to retain financing, (3) was so concerned about the company's viability that it monitored the company's financial health for months, (4) knew that the other fiduciaries had not even discussed the company's financial health, and (5) did nothing to protect the ESOP's assets until the stock had already lost the vast majority of its value. At an absolute minimum, such facts should raise genuine issues of material fact as to such a trustee's liability for failing to diversify the ESOP's investments.

The Court should grant certiorari in order to resolve the significant Circuit split on these issues and to set the proper standard for fiduciary and directed-trustee liability for failure to diversify an ESOP's investments.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DECIDED JUNE 28, 2006

IN THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Nos. 05-4005, 05-4317

JERRY SUMMERS, *et al.*, individually and on behalf of all others similarly situated,

Plaintiffs-Appellants, Cross-Appellees,

v.

STATE STREET BANK & TRUST COMPANY,

Defendant-Appellee, Cross-Appellant,

and

UAL CORPORATION ESOP COMMITTEE, *et al.*,

Defendants, Cross-Appellees.

Appeals from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 03 C 1537—Samuel Der-Yeghiayan, *Judge*

ARGUED APRIL 4, 2006—DECIDED JUNE 28, 2006.

Appendix A

Before POSNER, WOOD, and EVANS, Circuit Judges.

POSNER, *Circuit Judge*. At the end of 2002, when United Air Lines declared bankruptcy, its employees (both active and retired) owned more than half the airline's common stock through an ESOP (employee stock ownership plan). *In re UAL Corp.*, 412 F.3d 775, 777 (7th Cir.2005). ESOPs are subject to ERISA, the federal pension law, 29 U.S.C. §§ 1104(a)(2), 1107(b), (d)(6); *Armstrong v. LaSalle Bank National Ass'n*, 446 F.3d 728, 730 (7th Cir.2006), and this is a suit under ERISA. The plaintiffs represent a class consisting of United's employees. The principal defendant is State Street Bank & Trust, a cofiduciary of the UAL Corporation ESOP Committee. The Committee-which has six members, all appointed by the unions that represent United's employees-is the only fiduciary named in the plan. 29 U.S.C. § 1102(a)(1). The plan directs the Committee "to establish an investment policy and objective for the Plan, except that it is understood that the Plan is designed to invest exclusively in Company Stock." The Committee accordingly established a policy and goal of owning United stock, and appointed State Street to be the plan's trustee, that is, to manage the ESOP's assets, initially consisting of that stock. § 1103(a). The class charges State Street with imprudent management—specifically with failing to sell United stock as its market price plummeted en route to the airline's bankruptcy—and is appealing from the grant of summary judgment to State Street, which has in turn cross-appealed on an unrelated issue that we discuss at the end of this opinion.

State Street is what is called a "directed" trustee, because the Committee (the fiduciary named in the plan), in

accordance with the plan language that we have quoted, directed State Street to invest the ESOP's assets exclusively in stock of United Air Lines. Directed trustees are permitted by ERISA: if an ERISA plan "provides that the trustee or trustees are subject to the direction of a named fiduciary [in this case it is the UAL Corporation ESOP Committee] who is not a trustee, . . . the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to [ERISA]." 29 U.S.C. § 1103(a)(1); see *Maniace v. Commerce Bank, N.A.*, 40 F.3d 264, 267 (8th Cir.1994); *May Dept. Stores Co. v. Federal Ins. Co.*, 305 F.3d 597, 599 (7th Cir.2002); *LaLonde v. Textron, Inc.*, 369 F.3d 1, 5 (1st Cir.2004). Like other ERISA trustees, a directed trustee has a statutory duty of prudence. § 1104(a)(1)(B). But as an ESOP fiduciary, he does not have the further (really, the included) duty to diversify the trust assets, § 1104(a)(1)(C)—we call it "included" in the duty of prudence because diversification is normally an essential element of prudent investing by a fiduciary. *Armstrong v. LaSalle Bank National Ass'n, supra,* 446 F.3d at 732. A directed trustee appointed under an ERISA plan does not have that duty because the very purpose of an ESOP is to invest in a single stock, that of the employer of the ESOP's participants.

We must first decide whether a directed trustee of an ESOP has any fiduciary duty with respect to the choice of trust assets, specifically any duty ever to replace the employer's stock-the normal holding of an ESOP-with some other security. The *Maniace* case that we cited, along with *Herman v. NationsBank Trust Co.*, 126 F.3d 1354, 1361-62 (11th Cir.1997), says no, but *FirsTier Bank, N.A. v. Zeller,*

16 F.3d 907, 911 (8th Cir.1994), says yes, as does *In re WorldCom, Inc. ERISA Litigation,* 354 F.Supp.2d 423, 444-45, 449 (S.D.N.Y.2005). The split reflects a confusing statutory picture. One provision of ERISA states that the directed trustee cannot be liable for obeying the directions of the fiduciary named in the plan, § 1105(b)(3)(B), but other provisions impose liability on a fiduciary for breaches of fiduciary duty by a cofiduciary if he knows of the breach and takes no reasonable efforts to prevent it, or if by his own failure to exercise prudence he enables the breach. §§ 1105(a)(2), (3). And recall that the directed trustee "shall be subject to *proper* directions of [the named] fiduciary which are made in accordance with the terms of the plan and *which are not contrary to [ERISA].*" § 1103(a)(1) (emphasis added). An imprudent direction cannot be a proper direction since the trustee has an express statutory duty of prudence.

The tension among these provisions is reflected in a pamphlet published by the Labor Department's Employee Benefits Security Administration, which affirms both that the directed trustee has a duty of prudence and that he has no "direct obligation to determine the prudence of a transaction" entrusted by the plan to another fiduciary. "Fiduciary Responsibilities of Directed Trustees" (Field Assistance Bulletin 2004-03, Dec. 17, 2004). "[D]irect" is the critical word, inviting us to resolve the tension by ruling that the trustee can disobey the named fiduciary's directions when it is plain that they are imprudent. (The Labor Department's pamphlet, as we'll see, is actually consistent with this approach.) The trustee physically controls the trust assets; knowingly to invest them imprudently or let them remain invested imprudently is irresponsible behavior for a trustee,

whose fundamental duty is to take as much care with the trust assets as he would take with his own property. He is "an agent who is required to treat his principal with utmost loyalty and care-treat him, indeed, as if the principal were himself." *Pohl v. National Benefits Consultants, Inc.*, 956 F.2d 126, 128-29 (7th Cir.1992). And although the creator of an ordinary trust may be able to include a provision in the trust instrument excusing the trustee from complying with the prudent-man rule, John H. Langbein, "The Contractarian Basis of the Law of Trusts," 105 *Yale L.J.* 625, 659-60 (1995), ERISA as we have seen expressly imposes the duty of prudence on directed trustees and forbids them to comply with directions of the fiduciary named in the plan that are not "proper." That is why *Kuper v. Iovenko*, 66 F.3d 1447, 1457 (6th Cir.1995), holds that an ERISA plan "may not be interpreted to include a per se prohibition against diversifying an ESOP."

Which brings us to the particulars of this case. The plaintiffs argue that State Street violated its fiduciary duty by failing to sell United stock held by the ESOP until the eve of United's bankruptcy. State Street knew long before then, if the plaintiffs are to be believed, that the UAL Corporation ESOP Committee, the named fiduciary, had unreasonably refused to deviate from the plan and diversify the ESOP's holdings or take other measures to reduce the looming risk to the employee-shareholders. The following chart traces the ups and downs (mostly downs) of United's

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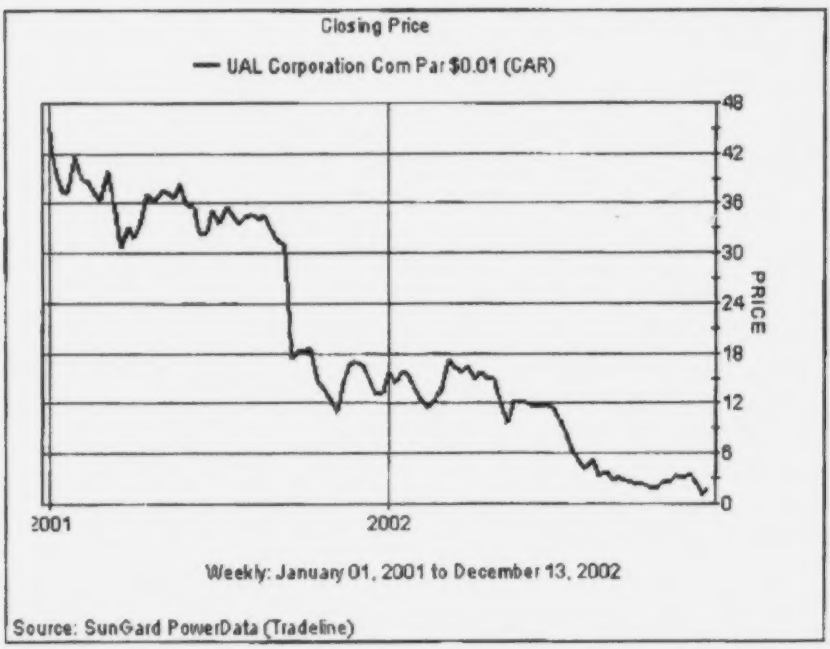
stock price between January 1, 2001, and December 9, 2002, when United declared bankruptcy:



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The price of United stock, which on September 10, 2001, was already 25 percent below the price at the beginning of the year, dropped almost 50 percent more in the immediate aftermath of the September 11, 2001, terrorist attacks. The following month, United's CEO sent a gloomy letter to all its employees which said that the company was "in a struggle just to survive" and was not yet in "a financial position that will allow us to continue operating," that it was "hemorrhaging money," and unless the "bleeding [was] stopped . . . United will perish sometime next year." The price of United stock fell another 20 percent in the two days after the publication of the letter.

The price continued falling, though with occasional upticks, and the financial press began speculating on the possibility of bankruptcy. State Street observed the decline with anxiety, but not until August 15, 2002-by which time the price had fallen to $2.70-did it notify the UAL Corporation ESOP Committee that it might be imprudent for the ESOP to continue holding United stock. In response to this warning the Committee authorized State Street to sell the stock, and it began doing so on September 27. By that time, however, the price had fallen to $2.36. The plaintiffs argue that State Street should have started selling within 30 days after the October 2001 letter of United's then-CEO and that had it done so the ESOP would have avoided $540 million in losses.

The plaintiffs say the letter should have alerted State Street that United was going into the tank. That is wrong. After the market "read" the letter, it valued United stock at $15.05 a share. Had the market thought that United would

be bankrupt by the end of 2002, it would not have priced its stock that high in October 2001, implying a market capitalization for the company of more than $800 million. A trustee is not imprudent to assume that a major stock market (United was traded on the New York Stock Exchange) provides the best estimate of the value of the stocks traded on it that is available to him. *In re UAL Corp., supra,* 412 F.3d at 777-78; see *Basic Inc. v. Levinson,* 485 U.S. 224, 247, 108 S.Ct. 978, 99 L.Ed.2d 194 (1988); *In re Hovis,* 356 F.3d 820, 823-24 (7th Cir.2004); *Feder v. Electronic Data Systems Corp.,* 429 F.3d 125, 138 (5th Cir.2005); Burton G. Malkiel, "Reflections on the Efficient Market Hypothesis: 30 Years Later," 40 *Financial Rev.* 1 (2005). At *any* price at which a sale takes place, the buyer thinks he's getting a bargain, or at least a reasonable deal-otherwise he wouldn't buy. Some investors, it is true, consistently beat the market, but few of them are trustees; it would be *hubris* for a trust company like State Street to think it could predict United's future more accurately than the market could, and preposterous for a committee of union officials (the named fiduciary) to challenge the market's valuation. Nor was State Street duty-bound to offer the Committee's members a tutorial on the obligations of an ERISA trustee; the Committee had its own lawyers for that.

Thus, at *every* point in the long slide of United's stock price, that price was the best estimate available either to State Street or to the Committee of the company's value, *In re UAL Corp., supra,* 412 F.3d at 777-78, and so neither fiduciary was required to act on the assumption that the market was overvaluing United. See *Wright v. Oregon Metallurgical Corp.,* 360 F.3d 1090, 1099 (9th Cir.2004);

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Kuper v. Iovenko, supra, 66 F.3d at 1460; *In re WorldCom, Inc. ERISA Litigation, supra*, 354 F.Supp.2d at 447. What is true, however, though largely (and fatally) ignored by the plaintiffs and mistakenly denied by State Street's lawyers in this court (State Street itself we assume knows better), is that the fall in the market price of United was increasing the risk borne by the owners of the stock, the participants in the ESOP. There is always risk, in the sense of variance of returns, to owning common stock, because the fortunes of a company are uncertain and the stockholders, unlike bondholders and other owners of the company's debt, do not have a fixed entitlement; they are the residual risk bearers. Some companies, however, are riskier than others. Of particular relevance to this case, the higher the ratio of fixed-interest debt to equity is, the riskier is the position of the equity holders (the common stockholders). If a company has no debt, a 5 percent increase in the company's value will increase shareholder equity by 5 percent, and a 5 percent decrease in the company's value will decrease shareholder equity by 5 percent. But if the company has a 1:1 debt-equity ratio, a 5 percent increase in the company's value will increase shareholder equity by 10 percent (.05/.50) and a 5 percent decrease in the company's value will decrease shareholder equity by 10 percent. As the value of United, as reckoned by the stock market, plummeted, the airline's debt-equity ratio soared because its debt wasn't decreasing, and this created an acute threat of bankruptcy.

Such a threat would be of little moment to people who held United stock as part of a diversified portfolio, because the risks of the various components of such a portfolio tend to cancel out; that is the meaning and objective of

diversification. *The Modern Theory of Corporate Finance* 6 (Clifford W. Smith, Jr., ed., 2d ed.1990). Probably, however, shares of United stock were the principal financial assets of most of United's employee-shareholders-at least those who, unlike pilots, have modest salaries-and hence their principal source of retirement income. And probably most of those non-wealthy employee-shareholders were risk averse; that is, they would prefer $10,000 certain to a 1 percent chance of obtaining $1 million, even though these are actuarial equivalents. They would be especially risk averse with regard to provision for their retirement, where they would be more dependent on their financial assets since they would no longer have earned income. Being risk averse, they would have preferred that the bulk of their financial assets not be invested in a single stock that, while worth as much as its market valuation (as far as anyone not possessing inside information could know), was extremely risky. "Because the value of any single stock or bond is tied to the fortunes of one company, holding a single kind of stock or bond is very risky. By contrast, people who hold a diverse portfolio of stocks and bonds face less risk because they have only a small stake in each company." N. Gregory Mankiw, *Principles of Economics* 546 (1998). That is why ERISA fiduciaries have a duty of diversification as part of their overall duty of prudence-unless as in this case they are directed pursuant to an ESOP to invest everything in stock of the participants' employer.

The employee-shareholders' total wealth included not only their stake in the ESOP but also-and for those not yet retired or approaching retirement this was probably more important-their expected earnings and fringe benefits as

employees of United. The financial distress that pushed United's stock price down also jeopardized that expected wealth (insofar as United employees could not expect to land equally good jobs at other companies) and so depressed the employee-shareholders' overall wealth by more than the fall in the price of the stock. Brett McDonnell, "ESOP's Failures: Fiduciary Duties When Managers of Employee-Owned Companies Vote to Entrench Themselves," 2000 *Colum. Bus. L.Rev.* 199, 207 (2000). State Street's lawyers thus miss the point in arguing that American Airlines was on the verge of bankruptcy too but managed to avoid it and so might United have done so. Someone who owned American Airlines stock, and would have wanted but was unable to diversify, would have been bearing unwanted risk during American's period of peril.

But because an ESOP is at once a permissible form of ERISA trust and nondiversified by definition, the trustee (along with the named fiduciary) is in an awkward position. If he diversifies he violates the plan, but if he doesn't diversify he may be imposing unwanted risk on the employee-shareholders-for it is unrealistic to suppose that the ESOP form was chosen because the employees *wanted* to bear unnecessary risk. The goal of an ESOP is to give employees not the thrills of gambling but a larger stake in the company's fortunes, see, e.g., *United States v. McCord*, 33 F.3d 1434, 1440 n. 6 (5th Cir.1994), in hopes of "broadening ownership of capital within a capitalist system" to the end of "encouraging capital formation through an improved form of finance, improved management-labor relations, and increased productivity." McDonnell, *supra*, at 220-21. *Why* Congress thought it appropriate to stimulate the adoption

of this business form by giving companies tax breaks rather than allowing the free market to determine the merits of the form is a separate question but not one we need answer in order to decide this case, although it is pertinent to note that one of the goals *not* sought to be achieved by the ESOP form is the funding of pension benefits. Michael A. Conte & Jan Svejnar, "The Performance Effects of Employee Ownership Plans," in *Paying for Productivity* 143, 143-44 (Alan S. Blinder ed.1990). It is a goal that the form is ill suited to attain because of its underdiversification.

The tension between the goal of protection against risk and the goal of a portfolio dominated by a single stock is not acute if the participants in the ESOP have adequate sources of income or wealth that are not correlated with the risk of that stock, so that the ESOP is not their primary financial asset. But if they don't have substantial other wealth the goals cannot be reconciled, though they can be compromised by requiring fiduciaries to begin diversifying the ESOP's assets at the point at which an increase in the riskiness of the assets, had it been foreseen, would have induced the creators of the ESOP either to have not created it at all or to have required at least partial diversification. (We say *begin* diversifying because if the stock held by the ESOP is a very large fraction of the outstanding stock of the employer, as in this case, the sell-off would have to be gradual in order to avoid precipitating a sharp drop in price, Louis K. Chan & Josef Lakonishok, "The Behavior of Stock Prices Around Institutional Trades," 50 *J. Finance* 1147, 1147-48 (1995); the market does not treat the stocks of different companies as being perfectly substitutable. Thus, State Street had a policy of limiting any day's sales of a given stock to 30

percent of the volume of sales that day.) Or, as *Kuper v. Iovenko, supra,* 66 F.3d at 1459, puts it, "the plaintiff must show that the ERISA fiduciary could not have reasonably believed that the plan's drafters would have intended under the circumstances that he continue to comply with the ESOP's direction that he invest exclusively in employer securities." See also *Moench v. Robertson,* 62 F.3d 553, 571-72 (3d Cir.1995).

In *Steinman v. Hicks,* 352 F.3d 1101 (7th Cir.2003), we noted a situation in which the duty of prudence could require diversification of an ESOP's holdings: if the "ESOP was [the employees'] principal retirement asset ... and was entirely invested in the stock of their employer ..., and their employer was bought in a stock-for-stock deal-so that all the assets of the ESOP became stock in the acquirer by a company that had a much higher debt-equity ratio than their (former) employer and as a result its stock price was much more volatile and its bankruptcy risk greater. Then, *even if the trustees did not predict the company's 'impending collapse,'* they might be required in the interest of the participants either to diversify the plan's stockholdings or to exchange the ... stock for Treasury bills." *Id.* at 1106 (emphasis added, citation deleted). The source of the duty to diversify would not be the trustees disagreement with the market valuation (their failure to predict the company's impending collapse), but the excessive risk imposed on employee-shareholders by the rise in the debt-equity ratio of the employer's stock as a result, in the example given in *Steinman,* of a merger and in our case of a plummeting stock price. How excessive would depend in the first instance on the amount and character of the employees' other assets, for, as we have already indicated,

it is the riskiness of one's portfolio, not of a particular asset in the portfolio, that is important to the risk-averse investor.

The plaintiffs never sought to explore these issues. So even if the methods of litigation could feasibly determine the point at which the ESOP trustee should sell in order to protect the employee-shareholders against excessive risk, the plaintiffs have made no effort to establish that point. They think that what State Street did wrong was to fail to second-guess the market; in fact what State Street may well have done wrong was to delay selling its United stock until too late to spare the employee-shareholders from bearing inordinate risk. Of course, if State Street had sold earlier and the stock had then bounced back, as American Airlines' stock did, State Street might well have been sued by the same plaintiffs, though the analysis presented in this opinion would have bailed it out.

There has thus been a failure of proof. But the plaintiffs can take some solace from the fact that determining the "right" point, or even range of "right" points, for an ESOP fiduciary to break the plan and start diversifying may be beyond the practical capacity of the courts to determine. The Department of Labor pamphlet that we cited earlier states that a directed trustee may have a duty to sell "where there are clear and compelling public indicators, as evidenced by an 8-K filing with the Securities and Exchange Commission (SEC), a bankruptcy filing or similar public indicator, that call into serious question a company's viability as a going concern." U.S. Dept. of Labor, *supra,* at 5-6. That is not an administrable standard; note the hedge in "may" and the fact that selling when bankruptcy is declared will almost certainly be too late.

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The time may have come to rethink the concept of an ESOP, a seemingly inefficient method of wealth accumulation by employees because of the underdiversification to which it conduces (though remember that what is important is the diversification of the employee's entire asset portfolio, including his earning capacity, rather than whether an individual asset is diversified). The tax advantages of the form do not represent a social benefit, but merely a shift of tax burdens to other taxpayers. Nor are we aware of an argument for subsidizing the ESOP form, as the tax law does, rather than letting the market decide whether it has economic advantages over alternative forms of business structure. As for the notion that having a stake in one's employer will induce one to be more productive, the evidence for such an effect-see "Motivating Employees with Stock and Involvement," *NBER Website*, Apr. 25, 2006, http:// www.nber.org /digest/may04/ w10177.html; Joseph Blasi, Michael Conte & Douglas Kruse, "Employee Stock Ownership and Corporate Performance Among Public Companies," *50 Indus. & Lab. Rel. Rev.* 60 (1996)-is weak and makes no theoretical sense. An employee has no incentive to work harder just because he owns stock in his employer, since his efforts, unless he is a senior executive, are unlikely to move the price of the stock. Nor is employee stock ownership likely to forge sentimental ties between employees and employers that might cause the former to work harder, although it may alleviate union pressures for wages or benefits that would jeopardize solvency.

A second ground of appeal argued by the plaintiffs is that the district judge should not have prevented their expert witness, Lucian Morrison, from testifying about State Street's

prudence or lack thereof in failing to sell United stock sooner. The judge thought Morrison unqualified because he lacks either a degree in economics or experience with bankruptcy. That was error. Morrison is a highly experienced trust officer and as such qualified to testify about State Street's management of the assets of the United ESOP. "Rule 702 [of the Federal Rules of Evidence] specifically contemplates the admission of testimony by experts whose knowledge is based on experience." *Walker v. Soo Line R.R.*, 208 F.3d 581, 591 (7th Cir.2000); see also *Smith v. Ford Motor Co.*, 215 F.3d 713, 718 (7th Cir.2000); *Hangarter v. Provident Life & Accident Ins. Co.*, 373 F.3d 998, 1015-16 (9th Cir.2004). But the error is harmless. Morrison was planning to testify that State Street should have seen the handwriting on the wall back in October or, at the latest, November of 2001. That is an echo of the argument by the plaintiffs' lawyers that State Street should have outsmarted the market and is not a correct interpretation of the duty of prudent management of trust funds, whatever a trust officer might think.

State Street has filed a contingent cross-appeal, challenging a settlement between the plaintiffs and its cofiduciary, the UAL Corporation ESOP Committee. Since we are affirming the dismissal of the plaintiffs' claim against State Street, there is no imperative need to discuss the cross-appeal; it is academic unless this court sitting en banc, or the Supreme Court, reverses our decision in favor of State Street. But the oddity of the situation presented by that appeal calls for some comment. The Committee's members were insured, and the settlement gives the plaintiffs $5.2 million, the limit of the insurance policy after deduction of incurred and expected legal expenses. The settlement provides that if

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State Street is determined to be liable for some amount of damages, the judge shall determine its fault relative to the Committee's and State Street may then seek contribution from the Committee's members. Suppose that State Street was ordered to pay the plaintiffs $540 million and the judge decided that it and the Committee were equally at fault. Then State Street would be entitled to a contribution of $264.8 million ($540 / 2 = $270-$5.2 = $264.8) from the Committee. But the Committee's members, we are told by their lawyer, have no assets beyond the insurance policy out of which to satisfy a judgment. This is probably an exaggeration, but a slight one. Suppose improbably that the six members have a total of $4.8 million in personal assets that might be used to satisfy a judgment. Then State Street, even though adjudged only 50 percent responsible for the (supposed) wrongful injury to the plaintiffs, would have to pay almost the entire judgment-$530 million ($270 million + $270 million-$ 5.2 million (paid by insurance company)-$4.8 million (paid by the Committee members) = $530 million) out of $540 million.

The judge in approving the settlement entered an order in effect barring State Street from seeking anything from the Committee members beyond what personal assets they may have. The judge gave no reason for this action; if we may judge from the arguments of the parties' lawyers, either he thought this result "fair" or, as argued by the plaintiffs' lawyer, thought it would make no difference because State Street could in no event obtain from the Committee members money they don't have. But if this is what the judge thought, he was wrong. The members' unions have agreed to indemnify them. Therefore if State Street obtained a judgment

of $264.8 million (in our example) against the members, the unions would have to pay so much of that judgment as they, not the Committee members, could afford. (So we're surprised that the union has not sought to intervene in the suit.)

The problem for which bar orders or, as they are sometimes called, "settlement bars" are a suggested solution was explained recently in *Denney v. Deutsche Bank AG,* 443 F.3d 253, 273 (2d Cir.2006): "If a nonsettling defendant against whom a judgment had been entered were allowed to seek payment from a defendant who had settled, then settlement would not bring the latter much peace of mind. He would remain potentially liable to a nonsettling defendant for an amount by which a judgment against a nonsettling defendant exceeded a nonsettling defendant's proportionate fault. This potential liability would surely diminish the incentive to settle." But to the extent that the nonsettling defendant has a valid claim for contribution from the settling defendant, a bar order that extinguished that claim would encourage a race to settle (to the arbitrary disadvantage of the defendants as a group), since each settling defendant's liability would be capped at the amount of his settlement. This court, in a case not cited by the district judge, has declined to adopt the settlement-bar approach on the ground that the hearing necessary to determine the value of the nonsettling defendant's contribution claim would be cumbersome and therefore costly, and "as the costs of settlement rise closer to those of trial, the likelihood of settlement falls-maybe far enough to offset the incentive to settle that a defendant has who knows that settling will enable him to avoid all liability to the other tortfeasors." *Donovan v. Robbins,* 752 F.2d 1170, 1181 (7th Cir.1985).

The settlement-bar approach assumes, moreover, that there is a right of contribution, and it is unsettled whether ERISA defendants have such a right. *Lumpkin v. Envirodyne Industries, Inc.*, 933 F.2d 449, 464 n. 10 (7th Cir.1991); compare *Chemung Canal Trust Co. v. Sovran Bank/ Maryland*, 939 F.2d 12, 16-17 (2d Cir.1991) (yes, contribution), with *Kim v. Fujikawa*, 871 F.2d 1427, 1432-33 (9th Cir.1989) (no). We assumed in *Alton Memorial Hospital v. Metropolitan Life Ins. Co.*, 656 F.2d 245, 250 (7th Cir.1981), that they do, but did not actually discuss the question, which remains an open one in this circuit. This is not the case in which to close it, as it would not affect our result; we mention it merely in the hope of heading off such errors in the future.

The judgment in No. 05-4005 is affirmed, and appeal No. 05-4317 is dismissed.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B — MEMORANDUM OPINION OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED AND FILED OCTOBER 12, 2005

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 03 C 1537

JERRY R. SUMMERS and GEORGE T. LENORMAND, individually and on behalf of all others similarly situated,

Plaintiffs,

v.

UAL CORPORATION ESOP COMMITTEE, MARTY TORRES, BARRY WILSON, DOUG WALSH, IRA LEVY, DON CLEMENTS, CRAIG MUSA and STATE STREET BANK & TRUST COMPANY,

Defendants.

MEMORANDUM OPINION

SAMUEL DER-YEGHIAYAN, District Judge

This matter is before the court on the parties' motions for summary judgment and on Defendant State Street Bank and Trust Company's ("State Street") motion to exclude Plaintiffs' expert opinions and testimony. For the reasons stated below, we deny Plaintiffs' partial motion for summary

judgment, grant State Street's motion for summary judgment, and grant State Street's motion to exclude Plaintiffs' expert testimony.

BACKGROUND

Plaintiffs were all participants in the United Airlines Corporation Employee Stock Ownership Plan ("Plan"). According to Plaintiffs, United Airlines ("UAL") was in financial trouble in July 2001, and after September 2001, UAL's financial position worsened. Plaintiffs claim that from August 2001 to August 2002, UAL stock prices fell over 80 percent in value. Plaintiffs contend that until August 2002, neither Defendant UAL Corporation ESOP Committee ("Committee"), the named fiduciary of the Plan, nor Defendant State Street, the trustee of the plan, took appropriate actions to protect the Plan assets by diversifying the stock held by the Plan. It is further alleged by Plaintiffs that the Committee members were not aware of the fiduciary duties they owed to the Plan. In August 2002, UAL announced that it might seek bankruptcy protection.

According to Plaintiffs, in September 2002, State Street notified the Committee of its fiduciary duties and nine days later, on September 27, 2002, the Committee began selling the Plan's UAL stock. Plaintiffs claim that by September 27, 2002, the UAL stock had already dropped to $2.36 per share and the Plan had already lost approximately two billion dollars as a result of the decrease in the value of the stock. UAL subsequently filed for bankruptcy. UAL and the individual committee member Defendants have entered into a settlement agreement in this action and State Street remains

as an active Defendant. Plaintiffs have filed a partial motion for summary judgment and State Street has filed a motion for summary judgment.

LEGAL STANDARD

Summary judgment is appropriate when the record, viewed in the light most favorable to the non-moving party, reveals that there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c). In seeking a grant of summary judgment, the moving party must identify "those portions of 'the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any,' which it believes demonstrate the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986) (quoting Fed.R.Civ.P. 56(c)). This initial burden may be satisfied by presenting specific evidence on a particular issue or by pointing out "an absence of evidence to support the non-moving party's case." *Id.* at 325. Once the movant has met this burden, the non-moving party cannot simply rest on the allegations in the pleadings, but, "by affidavits or as otherwise provided for in [Rule 56], must set forth specific facts showing that there is a genuine issue for trial." Fed.R.Civ.P. 56(e). A "genuine issue" in the context of a motion for summary judgment is not simply a "metaphysical doubt as to the material facts." *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 586, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986). Rather, a genuine issue of material fact exists when "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*,

477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986); *Insolia v. Philip Morris, Inc.*, 216 F.3d 596, 599 (7th Cir.2000). The court must consider the record as a whole, in the light most favorable to the non-moving party, and draw all reasonable inferences that favor the non-moving party. *Anderson*, 477 U.S. at 255; *Bay v. Cassens Transport Co.*, 212 F.3d 969, 972 (7th Cir.2000).

DISCUSSION

I. Opinions and Testimony of Lucian Morrison

State Street moves to strike or exclude the opinions and testimony of Plaintiffs' expert witness Lucian Morrison ("Morrison"). Federal Rule of Evidence 702 provides the following:

> If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case.

Fed.R.Evid. 702. A court in evaluating expert testimony must apply the *Daubert* analysis. *Durkin v. Equifax Check Services, Inc.*, 406 F.3d 410, 420 (7 Cir.2005). Under such an analysis,

the court must first assess the reliability of the expert's testimony, considering whether "the proposed witness would testify to valid scientific, technical, or other specialized knowledge." *Id.* Secondly, the court must assess the relevance of the expert's testimony, considering whether the "testimony will assist the trier of fact." *Id.*; *see also Fuesting v. Zimmer, Inc.*, 421 F.3d 528, 535 (7 Cir.2005)(stating that an examination of an expert's credentials to determine if he possesses sufficient knowledge, skill, experience, training, or education is not in and of itself a sufficient analysis and that the "district court must also, in keeping with its gatekeeper's duty, assess the reliability of the *methodology* the expert has employed in arriving at his opinion"). Thus, the district court acts as a "gatekeeper with respect to testimony proffered under Rule 702 to ensure that the testimony is sufficiently reliable to qualify for admission." *Mihailovich v. Laatsch*, 359 F.3d 892, 918 (7 Cir.2004). In determining whether expert testimony is admissible, the court should also consider the following non-exhaustive list of factors: "(1) whether the theoretical framework or technique underlying the witness's testimony . . . is subject to verification through testing, (2) whether it has been subjected to peer review and publication, (3) what its known or potential rate of error is, (4) whether there are standards controlling its application, and (5) whether it is generally accepted within the relevant expert community." *Id.*

In the instant action, Plaintiffs seek to offer Morrison's opinion that UAL's bankruptcy was imminent in October 2001, and that Defendants failed to act prudently by neglecting to sell the UAL stock to protect the interests of the Plan participants. Morrison has prior experience acting

as a professional fiduciary and has managed bank and trust activities when working for several banking and trust companies. He has also served as a trustee for employee benefit plans. However, State Street correctly points out that Morrison's opinions range far beyond the proper actions of a fiduciary and delve into areas of bankruptcy, insolvency, economics, and the securities industry. Plaintiffs have not shown that Morrison possesses the requisite "knowledge, skill, experience, training, or education" in such specialized areas. Fed.R.Evid. 702. The bankruptcy of UAL and its surrounding circumstances are key factors in assessing State Street's actions. Morrison is wholly deficient to offer expert testimony regarding such matters. Although he has some experience that has touched on the areas of economics, the securities industry, and corporate bankruptcies, such experience is not sufficient to qualify him as an expert in such areas. The bankruptcy of UAL is such an integral part of the claims in the instant action that a complete and thorough understanding of such matters is crucial to making any sort of informed testimony concerning the propriety of Defendants' actions.

Morrison's lack of expertise in bankruptcy matters and related matters is illustrated by the deficiency in his methodologies utilized in forming his opinions in the instant action. Morrison attempts to sidestep the necessary detailed expert analysis of UAL's financial condition by relying on external factors and extraneous evidence, such as statements made in a letter by UAL's CEO. The trier of fact can read and analyze such letters without the assistance of an expert, and Morrison's speculation based on such evidence is nothing more than a guess. Morrison has not shown to the court that

he utilized any reliable tests or methodologies to support his opinions. Morrison has not shown, for example, that he has utilized a methodology commonly employed by experts in analyzing bankruptcy situations. Morrison did not conduct a financial analysis of UAL's books or apply any reliable methodology in arriving at his opinions. Instead, Morrison offers his own unsupported theories and conclusions, and offers nothing of benefit to the trier of fact. The trier of fact is presumed to be able to think and reason on its own. An expert is not employed in litigation to "think" for the trier of fact. Rather, an expert may only assist the trier of fact in its understanding of the facts and issues at hand. So called "experts" such as Morrison are not entitled to weigh in with their half-baked opinions in order to attempt to sway the trier of fact in its analysis.

Plaintiffs apparently recognize the impropriety of offering Morrison as an expert and, in an effort to salvage at least some of Morrison's testimony, Plaintiffs ask the court to not engage in a "wholesale exclusion" of Morrison's testimony. (Ans.Excl.13). However, we agree with State Street that Morrison's opinions offer virtually nothing to the trier of fact and his uneducated speculation presented under the cloak of an "expert" would only be prejudicial to State Street. Although Morrison claims to have experience and training in certain basic areas that are the focus of the instant action, his lack of expertise in such areas renders all of his conclusions suspect. Therefore, we grant State Street's motion to exclude the opinions and testimony of Morrison.

Appendix B

II. State Street's Motion For Summary Judgment

State Street moves for summary judgment on all claims brought against it. To start, the fiduciary duties under ERISA are explained in 29 U.S.C. § 1104, which provides the following:

> (a) Prudent man standard of care
>
> (1) Subject to sections 1103(c) and (d), 1342, and 1344 of this title, a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and--
>
> (A) for the exclusive purpose of:
>
> (i) providing benefits to participants and their beneficiaries; and
>
> (ii) defraying reasonable expenses of administering the plan;
>
> (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;
>
> (C) *by diversifying the investments of the plan so as to minimize the risk of large losses,* unless under the circumstances it is clearly prudent not to do so; and

> (D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter and subchapter III of this chapter.

29 U.S.C. § 1104(a)(emphasis added); *see also DeBruyne v. Equitable Life Assur. Soc. of U.S.*, 920 F.2d 457, 465 (7 Cir.1990)(stating that in assessing whether "investment strategies were prudent, . . . the ultimate outcome of an investment is not proof of imprudence" and that "[t]he fiduciary duty of care, . . . requires prudence, not prescience"). A breach of fiduciary claim can only be brought against a fiduciary recognized under ERISA. *Baker v. Kingsley*, 387 F.3d 649, 660 (7 Cir.2004); *see also Bowerman v. Wal-Mart Stores, Inc.*, 226 F.3d 574, 590 (7 Cir.2000)(quoting 29 U.S.C. § 1104(a)(1) for the proposition that "[u]nder ERISA, a fiduciary must 'discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries'"). In regard to monitoring a plan's investments, a fiduciary has a general "duty of prudence." *Steinman v. Hicks*, 352 F.3d 1101, 1106 (7 Cir.2003).

We begin our analysis by noting a key fact. As Plaintiffs acknowledge, State Street was required by the Plan documents to invest the Plan funds in UAL stock. State Street could have sold the UAL stock sooner only if it chose to override the Plan's provisions based upon extraordinary circumstances. (Ans. St. SJ 1). If State Street had chosen to sell the UAL stock sooner and that decision proved to be premature, State Street would have breached its fiduciary duty to follow the directions of the Plan.

Appendix B

State Street was a directed trustee pursuant to 29 U.S.C. § 1103(a). As the court explained in *In re WorldCom, Inc. ERISA Litigation*, 354 F.Supp.2d 423 (S.D.N.Y.2005), a "directed trustee has no duty to investigate the wisdom of [investment] choices or any obligation to render advice regarding the choices" and the trustee's fiduciary duty is essentially to ensure that the actions of a plan are in compliance with ERISA. *Id.* at 449. Both State Street and Plaintiffs argue that the holding in *In re WorldCom, Inc.* supports a finding in their favor. (St. St. SJ 8)(Ans. St. St. SJ 3). We agree with the court's reasoning in *In re WorldCom, Inc.* that "a directed trustee's knowledge that a company's 'stock price and profits were declining and that the company was undergoing a restructuring' is not sufficient to find a breach of a fiduciary duty where the trustee continued to invest plan funds in the company's stock as directed." *Id.* (quoting *Lalonde v. Textron, Inc.*, 369 F.3d 1, 7 (1st Cir.2004)). The directed trustee can only be held accountable when failing to act upon reliable and trustworthy information. *Id.* n. 25. Such information generally consists of "public indicators" that show "an imminent collapse, as opposed to long-term indicators that could, for example, forecast a company's future obsolescence." *Id.* It is important that a directed trustee only be required to act upon reliable information that shows an imminent collapse because otherwise a fiduciary could be cajoled into prematurely selling off an employer's securities. The fiduciary, for all its caution, would not "maintain the investment in the employer's securities," and "it may face liability for that caution," especially if the collapse scare proves to be unfounded and ultimately the "employer's securities thrive." *Moench v. Robertson*, 62 F.3d 553, 572 (3 Cir.1995).

Appendix B

Plaintiffs' contention that Defendants should have sold UAL stock in October 2001 is mainly based upon a letter written by UAL CEO James Goodwin ("Goodwin letter"). Plaintiffs contend that the letter clearly showed that UAL was facing imminent financial collapse. However, State Street has provided ample evidence that indicates that during the fall of 2001, UAL was not facing imminent financial collapse. We are not, as Plaintiffs suggest, simply giving more weight to State Street's position because they have presented more expert opinions in their favor. Although the opinions of Morrison, Plaintiffs' expert, are unreliable to such an extent that they cannot be presented to the trier of fact, we have not simply accepted the veracity of State Street's expert opinions in default. Instead, we have thoroughly examined all of the opinions and conclusions of all of the experts, and have analyzed each of the expert's conclusions individually. The evidence presented by State Street is such that no reasonable trier of fact could conclude that UAL was facing imminent bankruptcy in October 2001. Our conclusions would not be altered even if we had considered Morrison's testimony and opinions. For instance, the evidence undeniably shows that UAL had a realistic expectation of receiving the grants and loan funds that it sought. The evidence also clearly shows that UAL had a strong cash position and the market indicators did not show that UAL was facing imminent bankruptcy.

Plaintiffs misquote the Goodwin letter in order to make their point that Goodwin was signaling that UAL's bankruptcy was imminent. Plaintiffs claim that Goodwin stated that UAL would "'perish next year' - which was then only 10 weeks away." (Ans. St. SJ 1). Plaintiffs thus assert that such a statement meant that in October 2001 the

bankruptcy was a few months away at the beginning of 2002. However, in actuality, Goodwin stated in his letter that UAL would "perish *some time* next year," which clearly indicates that any such problems could very easily have been far off in 2002. (Goodwin Let. 1)(emphasis added).

Also, Plaintiffs attempt to pull quotes from the Goodwin letter out of context. There is no indication that the letter was intended to provide an anticipatory notification of the inevitability of UAL's bankruptcy. Rather, the letter was clearly, as State Street refers to it, a "rallying call to the employees and the unions to come to the bargaining table, warning that if they did not, and various other events (such as obtaining a loan) did not occur, UAL [might] 'perish.'" (St. SJ Mem. 10). Nowhere in the Goodwin letter did Goodwin indicate that bankruptcy was imminent. Rather, Goodwin stated that UAL might ultimately perish down the road if certain issues were not addressed. This is clear, for example, by Goodwin's reference to the fact that if UAL did not succeed in certain areas, UAL would "*eventually* run out of money." (Goodwin Let. 1)(emphasis added). There is certainly no indication of imminent financial collapse from an assertion that there "eventually" may be such a collapse. The fact that Goodwin was not seeking to broadcast the inevitable financial collapse is also evident from the positive manner in which the letter is concluded: "The sooner we get to breakeven, the sooner we'll remove the doubts about our future." (Goodwin Let. 2).

State Street also correctly points out that the mere fact that the UAL stock price fell after terrorist attacks in September 2001, did not mean that UAL was doomed at that

point to financial collapse. There were sufficient indications that UAL could recover from its setbacks, and Plaintiffs now in hindsight unfairly seek to hold State Street accountable for not foreseeing the future and for failing to foresee UAL's ultimate filing of bankruptcy. Plaintiffs also attempt to hold State Street liable as an investment manager. State Street concedes for the purposes of its summary judgment motion that it became an investment manager as of August 2002. However, the evidence clearly shows that State Street began to sell UAL stock within one month of becoming the investment manager. The evidence also clearly shows that any delay on the part of State Street was part of a well thought out investigation to determine the best course of action, as required of any fiduciary.

Plaintiffs also seek to hold State Street liable as a co-fiduciary for violating the duties of prudence and loyalty pursuant to 29 U.S.C. § 1105(a), for enabling the Committee members to breach their fiduciary duties. However, the vast array of evidence in this case shows that UAL was not facing imminent bankruptcy in the fall of 2001 and that State Street, as a co-fiduciary of the Committee, did not breach its fiduciary duties. No reasonable trier of fact could find otherwise. Also, State Street reasonably believed that the Committee was fulfilling its fiduciary obligations. It was the Committee that had the primary responsibility of monitoring the investments in the Plan. It is undeniable, based upon the evidence, that the Committee members understood their fiduciary duties, including the need to diversify the Plan investments. Plaintiffs have not provided any evidence that shows that State Street representatives were present during the entirety of all of the Committee meetings or during all

discussions between Committee members and their advisors. Plaintiffs also admit pursuant to Local Rule 56.1 that in the fall of 2001, the Committee's own attorneys, Bonnie Levitt and Marian Durkin, "did not believe that UAL's bankruptcy was imminent, and did not believe it necessary to advise their clients to override the Plan." (R St. SF 61). Plaintiffs contend that State Street should have done more to provide the Committee with advice and information. However, State Street was not obligated to act as legal counsel for the Committee. In fact, the Committee had retained its own legal counsel. The evidence unquestionably shows that State Street fulfilled all of its obligations to ensure that the Committee understood its fiduciary duties and its ability to sell UAL stock and kept the Committee adequately informed. The evidence also clearly shows that State Street adequately monitored and evaluated the UAL stock.

Plaintiffs also contend that State Street knew that the Committee members were presented with conflicting loyalties. However, Plaintiffs have not pointed to sufficient evidence that would enable a reasonable trier of fact to conclude that State Street should have recognized any such conflicts or that any such conflicts actually existed. State Street did nothing more than acknowledge potential conflicts and Plaintiffs have attempted to create such conflicts when none existed. Finally, Plaintiffs complain about the fact that State Street did not notify the Committee that UAL was placed on State Street's internal watch list. However, we agree with State Street that such information did not have to be disclosed by State Street, and thus Plaintiffs' argument in that regard is nothing more than a red herring. The fact that UAL was on the watch list merely indicated that State Street

was closely monitoring UAL and did not mean that UAL was facing imminent bankruptcy. The evidence shows that the Committee knew that State Street monitored the UAL stock, and there is no evidence that State Street ever attempted to conceal its monitoring of that stock. Therefore, we grant State Street's motion for summary judgment. Also, based upon the above analysis and the evidence referred to above, we deny Plaintiffs' partial motion for summary judgment.

CONCLUSION

Based on the foregoing analysis, we grant State Street's motion for summary judgment and deny Plaintiffs' motion for partial summary judgment. We also grant State Street's motion to exclude Plaintiffs' expert opinions and testimony.

s/ Samuel Der-Yeghiayan
Samuel Der-Yeghiayan
United States District Court Judge

Dated: October 12, 2005

APPENDIX C — 29 U.S.C.S. § 1103

§ 1103. Establishment of trust

(a) Benefit plan assets to be held in trust; authority of trustees. Except as provided in subsection (b), all assets of an employee benefit plan shall be held in trust by one or more trustees. Such trustee or trustees shall be either named in the trust instrument or in the plan instrument described in section 402(a) [29 USCS § 1102(a)] or appointed by a person who is a named fiduciary, and upon acceptance of being named or appointed, the trustee or trustees shall have exclusive authority and discretion to manage and control the assets of the plan, except to the extent that—

(1) the plan expressly provides that the trustee or trustees are subject to the direction of a named fiduciary who is not a trustee, in which case the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to this Act, or

(2) authority to manage, acquire, or dispose of assets of the plan is delegated to one or more investment managers pursuant to section 402(c)(3) [28 USCS § 1102(c)(3)].

* * * *

APPENDIX D — 29 U.S.C.S. § 1104

§ 1104. Fiduciary duties

(a) Prudent man standard of care.

(1) Subject to sections 403(c) and (d), 4042, and 4044 [29 USCS § § 1103(c), (d), 1342, 1344], a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

(A) for the exclusive purpose of:

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of administering the plan;

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

(C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

(D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this title and title IV.

(2) In the case of an eligible individual account plan (as defined in section 407(d)(3) [29 USCS § 1107(d)(3)]), the diversification requirement of paragraph (1)(C) and the prudence requirement (only to the extent that it requires diversification) of paragraph (1)(B) is not violated by acquisition or holding of qualifying employer real property or qualifying employer securities (as defined in section 407(d)(4) and (5) [29 USCS § 1107(d)(4) and (5)]).

* * * *

APPENDIX E — 29 U.S.C.S. § 1105

§ 1105. Liability for breach by co-fiduciary

(a) Circumstances giving to liability. In addition to any liability which he may have under any other provision of this part [29 USCS § § 1101 et seq.], a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances:

(1) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission is a breach;

(2) if, by his failure to comply with section 404(a)(1) [29 USCS § 1104(a)(1)] in the administration of his specific responsibilities which give rise to his status as a fiduciary, he has enabled such other fiduciary to commit a breach; or

(3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

(b) Assets held by two or more trustees.

(1) Except as otherwise provided in subsection (d) and in section 403(a)(1) and (2) [29 USCS § 1103(a)(1) and (2)], if the assets of a plan are held by two or more trustees—

(A) each shall use reasonable care to prevent a co-trustee from committing a breach; and

(B) they shall jointly manage and control the assets of the plan, except that nothing in this subparagraph (B) shall preclude any agreement, authorized by the trust instrument, allocating specific responsibilities, obligations, or duties among trustees, in which event a trustee to whom certain responsibilities, obligations, or duties have not been allocated shall not be liable by reason of this subparagraph (B) either individually or as a trustee for any loss resulting to the plan arising from the acts or omissions on the part of another trustee to whom such responsibilities, obligations, or duties have been allocated.

(2) Nothing in this subsection shall limit any liability that a fiduciary may have under subsection (a) or any other provision of this part [29 USCS § § 1101 et seq.].

(3)(A) In the case of a plan the assets of which are held in more than one trust, a trustee shall not be liable under paragraph (1) except with respect to an act or omission of a trustee of a trust of which he is a trustee.

(B) No trustee shall be liable under this subsection for following instructions referred to in section 403(a)(1) [29 USCS § 1103(a)(1)].

* * * *

APPENDIX F — 29 U.S.C.S. § 1109

§ 1109. Liability for breach of fiduciary duty

(a) Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 411 of this Act [29 USCS § 1111].

(b) No fiduciary shall be liable with respect to a breach of fiduciary duty under this title if such breach was committed before he became a fiduciary or after he ceased to be a fiduciary.

APPENDIX G — 29 U.S.C.S. § 1132

§ 1132. Civil enforcement [Caution: See prospective amendment note below.]

(a) Persons empowered to bring a civil action. A civil action may be brought—

(1) by a participant or beneficiary—

(A) for the relief provided for in subsection (c) of this section, or

(B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2) by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 409 [29 USCS § 1109];

(3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this title or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this title or the terms of the plan;

(4) by the Secretary, or by a participant, or beneficiary for appropriate relief in the case of a violation of 105(c) [29 USCS § 1025(c)];

(5) except as otherwise provided in subsection (b), by the Secretary (A) to enjoin any act or practice which violates any provision of this title, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provision of this title;

(6) by the Secretary to collect any civil penalty under paragraph (2), (4), (5), (6), or (7) of subsection (c) or under subsection (i) or (l);

(7) by a State to enforce compliance with a qualified medical child support order (as defined in section 609(a)(2)(A) [29 USCS § 1169(a)(2)(A)]);

(8) by the Secretary, or by an employer or other person referred to in section 101(f)(1) [29 USCS § 1021(f)(1)], (A) to enjoin any act or practice which violates subsection (f) of section 101 [29 USCS § 1021(f)], or (B) to obtain appropriate equitable relief (i) to redress such violation or (ii) to enforce such subsection; or

(9) in the event that the purchase of an insurance contract or insurance annuity in connection with termination of an individual's status as a participant covered under a pension plan with respect to all or any portion of the participant's pension benefit under such plan constitutes a violation of part 4 of this title [subtitle] or the terms of the plan, by the Secretary, by any individual who was a participant or beneficiary at the time of the alleged violation, or by a fiduciary, to obtain appropriate relief, including the posting of security if necessary, to assure receipt by the participant or beneficiary of the amounts provided or to be provided by such insurance contract or annuity, plus reasonable prejudgment interest on such amounts.

* * * *

APPENDIX H — FIELD ASSISTANCE BULLETIN FROM THE U.S. DEPARTMENT OF LABOR, NO. 2004-03, DATED DECEMBER 17, 2004

U.S. Department of Labor

Employee Benefits Security Administration
Washington, D.C. 20210

FIELD ASSISTANCE BULLETIN NO. 2004-03

DATE: DECEMBER 17, 2004

MEMORANDUM FOR:
VIRGINIA C. SMITH,
DIRECTOR OF ENFORCEMENT
REGIONAL DIRECTORS

FROM: ROBERT J. DOYLE
DIRECTOR OF REGULATIONS
& INTERPRETATIONS

SUBJECT: FIDUCIARY RESPONSIBILITIES OF DIRECTED TRUSTEES

ISSUE: In the context of publicly traded securities, what are the fiduciary responsibilities of a directed trustee?

BACKGROUND

Many employee pension plans use directed trustees to carry out transactions according to instructions from a named fiduciary of the plan. During investigations of such transactions by the Department, difficult questions may arise

regarding the scope of the directed trustee's fiduciary duties. Recent court decisions, addressing this issue in the context of purchases and holdings of publicly traded employer securities in particular, have focused attention on the nature and scope of a directed trustee's fiduciary duties. This bulletin provides general guidance to EBSA regional offices regarding the Department's views on the responsibilities of directed trustees under ERISA, particularly with respect to directions involving employer securities.

FIDUCIARY STATUS OF DIRECTED TRUSTEE

Section 403(a) provides that a plan trustee "shall have exclusive authority and discretion to manage and control the assets of the plan." Section 3(21)(A) provides that a person is a fiduciary with respect to a plan "to the extent . . . he . . . exercises any authority or control respecting management or disposition of its assets." A plan trustee, therefore, will, by definition, always be a "fiduciary" under ERISA as result of its authority or control over plan assets. Not all trustees, however, have the same authority or discretion to manage or control the assets of a plan. In this regard, section 403(a) specifically recognizes that a trustee or trustees will have limited authority or discretion when:

> (1) the plan expressly provides that the trustee or trustees are subject to the direction of a named fiduciary who is not a trustee, in which case the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to this Act.

Appendix H

While section 403(a)(1) does not remove a directed trustee from section 3(21)'s purview, it significantly limits such a trustee's responsibilities as a plan fiduciary. As the district court in *In re Enron Corp. Securities, Derivative & ERISA Litig.*, 284 F. Supp. 2d 511, 601 (S.D. Tex. 2003), recognized:

> At least some fiduciary status and duties of a directed trustee are preserved, even though the scope of its exclusive authority and discretion to manage and control the assets of the plan' has been substantially constricted by the directing named fiduciary's correspondingly broadened role . . . .

The court in *In re WorldCom, Inc. ERISA Litig.*, 263 F. Supp. 2d 745, 762 (S.D.N.Y. 2003) also noted that, while the directed trustee provision serves as a limiting principle, "section 403(a) does not ... eliminate the fiduciary status or duties that normally adhere to a trustee with responsibility over ERISA assets." *See also FirsTier Bank, N.A. v. Zeller*, 16 F.3d 907, 9110 (8th Cir.), cert. denied sub nom, *Vercoe v. FirsTier Bank, N.A.*, 513 U.S. 871 (1994); *Herman v. NationsBank Trust Co.*, 126 F.3d 1354, 1361-62, 1370 (11th Cir. 1997).

The duties of a directed trustee under section 403(a)(1) are therefore significantly narrower than the duties generally ascribed to a discretionary trustee under common law trust principles.[1]

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1. It is assumed for purposes of this guidance that discretionary authority or control over plan assets, beyond that discussed herein as applicable to a person serving as a directed trustee under section 403(a)(1), has not been conferred upon a directed trustee under the terms of the plan, including trust and service provider agreements.

Appendix H

DETERMINING WHETHER A DIRECTION IS "PROPER"

Under section 403(a)(1), a directed trustee is subject to proper directions of a named fiduciary. For purposes of section 403(a)(1), a direction is proper only if the direction is "made in accordance with the terms of the plan" and "not contrary to the Act [ERISA]." Accordingly, when a directed trustee knows or should know that a direction from a named fiduciary is not made in accordance with the terms of the plan or is contrary to ERISA, the directed trustee may not, consistent with its fiduciary responsibilities, follow the direction.

In accordance with plan terms

Under section 403(a)(1), a directed trustee may not follow a direction that the trustee knows or should know is inconsistent with the terms of the plan. In order to make such determinations, directed trustees necessarily have a duty to request and review all the documents and instruments governing the plan that are relevant to its duties as directed trustee. Accordingly, if a directed trustee either fails to request such documents or fails to review the documents furnished in response to its request and, as a result of such failure, follows a direction contrary to the terms of the plan, the directed trustee may be liable for following such direction because the directed trustee had a duty to request and review pertinent plan documents and, therefore, should have known that the direction was not in accordance with the terms of the plan. If a directed trustee follows an improper direction, as would be the case where the purchase of a particular stock at the direction of the plan's named fiduciary is contrary to the plan's investment policy, the directed trustee may be liable

for a breach of its fiduciary duty to follow only proper directions.

It is the view of the Department that a direction is consistent with the terms of a plan if the documents pursuant to which the plan is established or operated do not prohibit the direction. It is also the view of the Department that if, in the course of reviewing the propriety of a particular direction, a directed trustee determines that the terms of the relevant documents are ambiguous with respect to the permissibility of the direction, the directed trustee should obtain a clarification of the plan terms from the fiduciary responsible for interpreting such terms in order to ensure that the direction is proper. In this regard, the directed trustee may rely on the interpretation of such fiduciary.

Not contrary to ERISA

Even when a direction is consistent with the terms of the plan, the direction may nonetheless fail to be a proper direction because it is contrary to ERISA. Under section 403(a)(1), a directed trustee may not follow a direction that the trustee knows or should know is contrary to ERISA. For example, the directed trustee cannot follow a direction that the directed trustee knows or should know would require the trustee to engage in a transaction prohibited under section 406 or violate the prudence requirement of section 404(a)(1). The following discussion further clarifies the duties of a directed trustee in this area.

Appendix H

Prohibited transaction determinations

A directed trustee must follow processes that are designed to avoid prohibited transactions. A directed trustee could satisfy its obligation by obtaining appropriate written representations from the directing fiduciary that the plan maintains and follows procedures for identifying prohibited transactions and, if prohibited, identifying the individual or class exemption applicable to the transaction. A directed trustee may rely on the representations of the directing fiduciary unless the directed trustee knows that the representations are false.

Prudence determinations

The named fiduciary has primary responsibility for determining the prudence of a particular transaction, whether the transaction involves buying, selling or holding particular assets. Accordingly, as the courts and the Department have long recognized, the scope of a directed trustee's responsibility is significantly limited. A directed trustee does not, in the view of the Department, have an independent obligation to determine the prudence of every transaction. The directed trustee does not have an obligation to duplicate or second-guess the work of the plan fiduciaries that have discretionary authority over the management of plan assets and does not have a direct obligation to determine the prudence of a transaction. *See In re WorldCom ERISA Litig.*, 263 F. Supp. 2d at 761; *Herman v. NationsBank Trust Co.*, 126 F.3d at 1361-62, 1371 (directed trustee does not have a direct obligation of prudence under ERISA section 404; its obligation is simply "to make sure" the "directions were

proper, in accordance with the terms of the plan, and not contrary to ERISA").

Duty to act on non-public information

The directed trustee's obligation to question market transactions involving publicly traded stock on prudence grounds is quite limited. The primary circumstance in which such an obligation could arise is when the directed trustee possesses material non-public information regarding a security. If a directed trustee has material non-public information that is necessary for a prudent decision, the directed trustee, prior to following a direction that would be affected by such information, has a duty to inquire about the named fiduciary's knowledge and consideration of the information with respect to the direction. For example, if a directed trustee has non-public information indicating that a company's public financial statements contain material misrepresentations that significantly inflate the company's earnings, the trustee could not simply follow a direction to purchase that company's stock at an artificially inflated price.

Generally, the possession of non-public information by one part of an organization will not be imputed to the organization as a whole (including personnel providing directed trustee services) where the organization maintains procedures designed to prevent the illegal disclosure of such information under securities, banking or other laws.[2] If, despite such

2. The Department expresses no view as to whether, or under what circumstances, other procedures established by an organization to limit the disclosure of information will serve to avoid the imputation of information to a directed trustee.

procedures, the individuals responsible for the directed trustee services have actual knowledge of material non-public information, the directed trustee, prior to following a direction that would be affected by such information, has a duty, as indicated above, to inquire about the named fiduciary's knowledge and consideration of the information with respect to the direction. Similarly, if the directed trustee performs an internal analysis in which it concludes that the company's current financial statements are materially inaccurate, the directed trustee would have an obligation to disclose this analysis to the named fiduciary before making a determination whether to follow a direction to purchase the company's security. The directed trustee would not have an obligation to disclose reports and analyses that are available to the public.

Duty to act on public information

Absent material non-public information, a directed trustee, given its limited fiduciary duties as determined by statute, will rarely have an obligation under ERISA to question the prudence of a direction to purchase publicly traded securities at the market price solely on the basis of publicly available information. Three considerations counsel in favor of this view: (1) markets generally are assumed to be efficient so that stock prices reflect publicly available information and known risks; (2) in the case of employer securities, the securities laws impose substantial obligations on the company, its officers, and its accountants to state their financial records accurately; and (3) ERISA section 404 requires the instructing fiduciary to adhere to a stringent

standard of care.[3] Furthermore, because stock prices fluctuate as a matter of course, even a steep drop in a stock's price would not, in and of itself, indicate that a named fiduciary's direction to purchase or hold such stock is imprudent and, therefore, not a proper direction.

In limited, extraordinary circumstances, where there are clear and compelling public indicators, as evidenced by an 8-K filing with the Securities and Exchange Commission (SEC), a bankruptcy filing or similar public indicator, that call into serious question a company's viability as a going concern,[4] the directed trustee may have a duty not to follow the named

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3. It should be noted that, in the case of an individual account plan, the diversification requirements of section 404(a)(1)(C) do not apply to the acquisition or holding of qualifying employer securities within the meaning of section 407(d)(5).

4. We note that section 409 of the Sarbanes-Oxley Act of 2002, 15 U.S.C. 78(m)(l), requires public companies to disclose "on a rapid and current basis" material information regarding changes in the company's financial condition or operations as the SEC by rule determines to be necessary or useful for the protection of investors or in the public interest. The SEC has recently updated its disclosure requirements related to Form 8-K, expanding the number of reportable events and shortening the filing deadline for most items to four business days after the occurrence of the event triggering the disclosure requirements of the form. 69 FR. 15594 (Mar. 25, 2004). Not all 8-K filings regarding a company would trigger a duty on the part of a directed trustee to question a direction to purchase or hold securities of that company. Only those relatively few 8-Ks that call into serious question a company's ongoing viability may trigger a duty on the part of the directed trustee to take some action.

fiduciary's instruction without further inquiry.[5] For example, if a company filed for bankruptcy under circumstances which make it unlikely that there would be any distribution to equity-holders, or otherwise publicly stated that it was unlikely to survive the bankruptcy proceedings in a manner that would leave current equity-holders with any value, the directed trustee would have an obligation to question whether the named fiduciary has considered the prudence of the direction.[6] It also is the view of the Department that, in situations where a fiduciary who is a corporate employee gives an instruction to buy or hold stock of his or her company subsequent to the company, its officers or directors, being formally charged by state or Federal regulators with financial irregularities, the directed trustee, taking such facts into account, may need to decline to follow the direction or may need to conduct an independent assessment of the transaction in order to assure itself that the instruction is consistent with ERISA.[7] If, however, an independent fiduciary was appointed

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5. A directed trustee's actual knowledge of media or other public reports or analyses that merely speculate on the continued viability of a company does not, in and of itself, constitute knowledge of clear and compelling evidence concerning the company sufficient to give rise to a directed trustee's duty to act.

6. Even under such circumstances, it might not be imprudent to purchase or hold stock in a distressed company in bankruptcy. There may be situations in which the plan's fiduciaries could reasonably conclude that the stock investment makes sense, even for a long-term investor, in light of the proposed restructuring of the company's debts or other factors.

7. Nothing in the text should be read to suggest that a directed trustee would have a heightened duty whenever a regulatory body opens an investigation of a company whose securities are the subject of a direction, merely based on the bare fact of the investigation.

to manage the plan's investment in company stock, a directed trustee could follow the proper directions of the independent fiduciary without having to conduct its own independent assessment of the transaction.

EFFECT OF QUESTIONING DIRECTIONS ON FIDUCIARY STATUS

It is the view of the Department that the nature and scope of a directed trustee's fiduciary responsibility, as discussed herein, does not change merely because the directed trustee, in carrying out its duties, raises questions concerning whether a direction is "proper" or declines to follow a direction that the directed trustee does not believe is a proper direction within the meaning of section 403(a)(1). For example, information provided to a named fiduciary concerning the prudence of a direction is not investment advice for purposes of ERISA §3(21)(A)(ii). Similarly, if a named fiduciary changes a direction in response to a directed trustee's inquiries or information, the directed trustee's fiduciary responsibility with respect to the changed direction remains governed by section 403(a)(1). The directed trustee does not become primarily responsible for the prudence of the direction.

CO-FIDUCIARY DUTIES

Under ERISA section 405(a)(1), a fiduciary is liable for the breach of another fiduciary if the fiduciary "participates knowingly" in the breach of the other fiduciary. Accordingly, if a directed trustee has knowledge of a fiduciary breach, the directed trustee may be liable as a co-fiduciary unless the

directed trustee takes reasonable steps to remedy the breach. Thus, if the directed trustee knew that the named fiduciary was failing to discharge its obligations in accordance with ERISA's requirements, it could not simply follow directions from the breaching fiduciary. Efforts to remedy a breach (or to prevent an imminent breach) may include reporting the breach to other fiduciaries of the plan or the Department of Labor.

CONCLUSION

Although its responsibilities are significantly limited under the statute, a directed trustee is a fiduciary under ERISA and must exercise its duties prudently and solely in the interest of the plan participants and beneficiaries. Particularly in the context of purchasing, selling or holding publicly traded securities on a generally recognized market, the trustee may follow the named fiduciary's directions absent extraordinary circumstance as discussed above.

Supreme Court, U.S.
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No. 06-439

IN THE

Supreme Court of the United States

JERRY SUMMERS, GEORGE T. LENORMAND, JEFFERY D. CRITES, LOUISE VAN RAENSBURG and JAMES E. SHAMBO, individually and on behalf of all others similarly situated,

Petitioners,

v.

STATE STREET BANK & TRUST COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Did the Seventh Circuit err in affirming the district court's grant of summary judgment, concluding Petitioners presented insufficient evidence to overcome the presumption that the directed trustee of an employee stock ownership plan fulfilled its fiduciary duty by following the directions of the named fiduciaries to remain invested in employer stock?

LIST OF PARTIES AND DISCLOSURE STATEMENT PURSUANT TO RULE 29.6

In addition to the parties identified in the caption, the following were parties in the consolidated appeal proceedings before the Seventh Circuit Court of Appeals: UAL Corporation Employee Stock Ownership Plan Committee, Marty Torres, Barry Wilson, Doug Walsh, Ira Levy, Don Clements, and Craig Musa.

Respondent State Street Bank & Trust Company ("State Street") is a wholly-owned subsidiary of State Street Corporation, a bank holding company with no other business.

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STATUTES AND OTHER PROVISIONS INVOLVED

Statutes at issue in this case include the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§ 1002(21)(A), 1102(a)(2) (Resp. App. A and B), 1103(a)(1), 1104(a)(1), 1109(a), and 1132(a) (Pet. App. C, D, F and G). Also at issue is U.S. Department of Labor Employee Benefits Security Administration, Fiduciary Responsibilities of Directed Trustees, Field Assistance Bulletin 2004-03 (Dec. 17, 2004) (Pet. App. H), Federal Rule of Civil Procedure 56(c) (Resp. App. C), and Seventh Circuit Rule 40(e) (Resp. App. D).

STATEMENT OF THE CASE

After UAL Corporation ("UAL")[1] declared bankruptcy at the end of 2002, the participants of the UAL employee stock ownership plan (the "Plan") sued the fiduciaries of the Plan, claiming the fiduciaries breached their duties under ERISA by failing to divest the Plan of UAL stock and to override the terms of the Plan, which required that the assets be invested exclusively in UAL stock, fourteen months prior to the bankruptcy filing. *Summers v. State Street Bank & Trust Co.*, 453 F.3d 404, 405 (7th Cir. 2006).

The ESOP Committee (the "Committee") and its members, the only named fiduciaries in the Plan, 29 U.S.C. § 1102(a)(2), settled with Petitioners. The remaining defendant and Respondent in these proceedings, State Street Bank & Trust Company ("State Street"), was the directed trustee and a co-fiduciary of the Plan.

The Plan's Trust Agreement (the "Trust Agreement") obligated State Street, as directed trustee, to follow the Committee's directions and gave State Street no discretion regarding the disposition of the Plan's assets.[2] The Trust

[1] UAL Corporation is the holding company whose primary subsidiary is United Airlines.

[2] R.Doc.130, Ex. 2, Ex. A (Trust Agreement at § 3.1).

Agreement required State Street to invest the assets of the trust fund "exclusively" in UAL stock at the "direction of the ESOP Committee."[3] Under the Trust Agreement, State Street had to follow the directions of the Committee as long as such direction was in accordance with the terms of the Plan, proper within the meaning of 29 U.S.C. § 1103(a), and not contrary to ERISA.[4]

State Street monitored the financial condition of its clients, including UAL, whose ESOPs held the respective client's stock ("Employer Securities"), irrespective of whether State Street was the named fiduciary or the directed trustee.[5] CitiStreet LLC ("CitiStreet") performed this monitoring function on State Street's behalf. CitiStreet had two committees that met regularly to review Employer Securities: the Fiduciary Committee and the Watchlist Committee. (The latter reported to the former.) If an Employer Security were deemed to be "at-risk," the Watchlist Committee placed it on a watchlist, to be reviewed more closely by the Watchlist Committee.[6]

On December 20, 2001, the Watchlist Committee placed UAL on the watchlist after evaluating information concerning UAL's financial condition, including: an October 17, 2001 letter from then-Chief Executive Officer James Goodwin to UAL's employees asking for wage concessions following the tragic events of September 11, 2001 (the "Goodwin Letter"); analyst reports; and a benchmark deviation report showing that UAL stock deviated from its established benchmark three times within a four-week period.[7]

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[3] R.Doc.130, Ex. 2, Ex. A (Trust Agreement at § 3.3).

[4] R.Doc.130, Ex. 2, Ex. A (Trust Agreement at § 3.6.3).

[5] R.Doc.124 (State Street Statement of Undisputed Facts in support of Summary Judgment ("SUF") ¶ 4); R.Doc.130, Ex. 11 (Declaration of Susan Daniels ("Daniels Decl."), ¶ 22).

[6] R.Doc.124 (SUF ¶ 6); R.Doc.130, Ex. 11 (Daniels Decl., ¶¶ 7-20).

[7] R.Doc.124 (SUF ¶ 11); R.Doc.130, Ex. 11 (Daniels Decl.,¶ 23), Ex. C (December 20, 2001 Watchlist Minutes).

Petitioners argue placement on the watchlist was insufficient and that, following issuance of the Goodwin Letter, State Street should have overridden the Plan, Trust Agreement, and the directions of the named fiduciary, and should have sold the UAL stock held by the ESOP. Petitioners contend the Goodwin Letter was a clear "sign" or "warning" that UAL would shortly file bankruptcy. State Street did not agree.

The Goodwin Letter was issued in the context of labor negotiations and was understood by many, including analysts and the machinists' union, to be a negotiating ploy.[8] The Goodwin Letter was a rallying call to the employees and the unions to come to the bargaining table and threatened that if various events and agreements were not reached, UAL would "perish some time next year."[9] The phrase "some time next year" "clearly indicates that any such problems could very easily have been far off in 2002." *Summers v. UAL Corp. ESOP Comm.*, No. 03 C 1537, 2005 U.S. Dist. LEXIS 23918, at *17 (N.D. Ill. Oct. 12, 2005). Moreover, the Goodwin Letter concluded in an upbeat and hopeful manner: "The sooner we get to break even, the sooner we'll remove the doubts about our future." The machinists' union sharply criticized the letter.[10] Goodwin subsequently resigned, and his successor Jack Creighton immediately and unequivocally stated that UAL was not considering bankruptcy.[11]

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[8] R.Doc.124 (SUF ¶ 34); R.Doc.130, Ex. 8 (Declaration of Gary Sbona ("Sbona Decl."), Ex. A (Expert Report of Gary Sbona ("Sbona Report"), ¶ 27); R.Doc.158 (Plaintiffs' Response To State Street's Statement of Undisputed Facts ("PR") ¶ 37).

[9] R.Doc.130, Ex.2 (Declaration of Marian M. Durkin ("Durkin Decl.") ¶ 42), Ex. E ("Goodwin Letter").

[10] R.Doc.129, Exhibits to UAL ESOP Committee Defendants' Statement of Undisputed Facts ("Committee Def.") Ex. 41 (Wash. Post Article, undated).

[11] R.Doc.129, Committee Def. Ex. 39 (WSJ.Com Article, 10/29/2001).

During the next nine months, the Watchlist Committee actively monitored UAL's performance and regularly provided the Fiduciary Committee with benchmark deviation reports on UAL's stock.[12] While State Street monitored the UAL stock, it knew that the named fiduciaries on the Committee also reviewed financial information about UAL. State Street was aware that Houlihan Lokey Howard & Zukin ("Houlihan Lokey") (outside consultants) presented investment advice to the Committee, including copies of annual valuation reports, analyses of UAL's financial condition, and presentations regarding the value of UAL stock.[13] The oral and written presentations included summaries of analyst recommendations, a general industry and economic overview, and information about UAL's financial status.[14]

Of the approximately 110 analyst reports dated from October 17, 2001 through August 13, 2002 (including all those Petitioners cite),[15] none recommended selling during the relevant time period and at least one recommended "accumulate."[16] None said UAL's bankruptcy was highly probable and none said bankruptcy was going to occur in the near or short term.[17] One

[12] R.Doc.124 (SUF ¶ 12); R.Doc.130, Ex. 11 (Daniels Decl., ¶¶ 24-26), Ex. D-F (Watchlist and Fiduciary Committee Minutes; Deviation Reports).

[13] R.Doc.130, Ex. 9 (Declaration of Ben Buettell ("Buettell Decl."), ¶¶ 9-12); R.Doc.167 (State Street's Statement of Additional Facts In Opposition to Plaintiffs' Motion For Partial Summary Adjudication ("SAF"), ¶ 91).

[14] R.Doc.167 (SAF ¶ 91); R.Doc.130, Ex. 9 (Buettell Decl., ¶¶ 17-20), Ex. D-I (Draft Presentation & Draft Discussion Materials); Ex. 10 (Declaration of Kelly Q. Driscoll ("Driscoll Decl.") ¶ 10).

[15] R.Doc.167 (SAF ¶ 71); R.Doc.130, Ex. 15 (Declaration of Ronald S. Kravitz ("Kravitz Decl."), ¶¶ 6-7), Ex. F (Analyst Reports).

[16] R.Doc.167 (SAF ¶ 66); R.Doc.130, Ex. 15 (Kravitz Decl., ¶¶ 6-7), Ex. F (Analyst Reports).

[17] R.Doc.167 (SAF ¶ 71); R.Doc.130, Ex. 15 (Kravitz Decl., ¶¶ 6-7), Ex. F (Analyst Reports).

commentary specifically noted that the Goodwin Letter did not mean UAL was facing bankruptcy.[18]

As part of its monitoring duties, State Street, CitiStreet, and Houlihan Lokey met with a representative of UAL's investor relations department in April 2002, to evaluate UAL's progress in implementing its recovery plan.[19] In May 2002, the Fiduciary Committee issued a report noting that UAL had billions of dollars in reserves; analyst reports recommended a "buy" or "hold"; benchmark deviation reports remained favorable; and UAL was actively involved in ongoing negotiations with its unions, the primary goal of which was to reduce costs.[20] Although the report stated that there was a "high risk" that UAL would not be able to gain the "wage concessions" it was requesting of the unions, it also noted that "[a]t the end of June, 2002, UAL stated its daily losses were significantly lower than in the First Quarter" of 2002.[21]

"In a sharp reversal from its previous stance," UAL issued a press release on August 14, 2002, warning that it may file bankruptcy that autumn unless "employees and vendors agree to dramatic wage and cost concessions."[22] State Street responded immediately by requesting a meeting with the Committee.[23]

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[18] R.Doc.16, (SAF ¶ 65); R.Doc.130, Ex. 15 (Kravitz Decl., ¶¶ 6-7), Ex. F (Analyst Reports).

[19] R.Doc.124 (SUF ¶ 15); R.Doc.130, Ex. 11 (Daniels Decl.,¶ 26).

[20] R.Doc.124 (SUF ¶ 16); R.Doc.130, Ex. 11 (Daniels Decl., ¶¶ 27-28), Ex. H (May, 2002, State Street Report).

[21] R.Doc.130, Ex. 11 (Daniels Decl.,¶¶ 27-28), Ex. H (May, 2002, State Street Report).

[22] R.Doc.184, Plaintiffs' Exhibits In Opposition To State Street's Motion For Summary Judgment ("Pfs.' Ex.") 58 (Chicago Tribune Article, 8/15/02).

[23] R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 15); Ex. 9 (Buettel Decl., ¶ 16); Ex. 2 (Durkin Decl., ¶ 46).

On August 20, 2002, State Street and the Committee met. State Street asked the Committee whether it had come to any conclusions about the prudence of continuing to hold UAL stock.[24] The Committee's lawyers attended this meeting, as well as the previous meetings, and knew that the Committee had an obligation to consider whether it was prudent to retain UAL stock in the Plan. State Street did not have any reason to believe that the Committee and its lawyers had not previously discussed selling the UAL stock in the Plan.[25]

On August 30, 2002, the Committee responded, on the advice of its counsel, by asking State Street to become Investment Manager of the Plan.[26] State Street agreed and became Investment Manager effective September 7, 2002.[27] Shortly thereafter, State Street evaluated alternative investments for the Plan and consulted with Houlihan Lokey, investment bankers, investment analysts, union representatives (who expressed optimism about labor negotiations), and UAL's Chief Financial Officer (who was hopeful that a solution could be found).[28]

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[24] R.Doc.124 (SUF ¶ 18); R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 17).

[25] R.Doc.124 (SUF ¶¶ 59-60, 62); R.Doc.130, Ex. 6 (Declaration of Bonnie Levitt ("Levitt Decl."), ¶¶ 7, 12-14, 20), Ex. 12 (Declaration of Marty Torres ("Torres Decl."), ¶¶ 14-21), Ex. 13, (Declaration of Barry Wilson ("Wilson Decl."), ¶¶ 15-22).

[26] R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 20); Ex. 2 (Durkin Decl., ¶¶ 45-49); Ex. 4 (Declaration of Wayne Jacobsen ("Jacobsen Decl."), ¶¶ 16-17), Ex. B (8/29/02 Committee minutes).

[27] R.Doc.124 (SUF ¶ 19); R.Doc.130, Ex. 10 ((Driscoll Decl., ¶ 20); Ex. 2 (Durkin Decl., ¶ 49), Ex. H (Investment Manager Engagement Letter).

[28] R.Doc.124 (SUF ¶ 20); R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 25) and Ex. B; Ex. 9 (Buettell Decl., ¶ 19), Ex. F (Draft Discussion Materials).

On September 25, 2002, State Street determined that it was no longer prudent for the Plan to hold UAL stock and authorized appropriate actions to sell the stock as soon as possible.[29] On September 27, 2002, State Street began divesting the Plan of UAL stock.[30] On December 9, 2002, a few days after the Air Transportation Stabilization Board loan was denied, UAL filed its chapter 11 bankruptcy petition.[31] As a result of State Street's efforts, the Plan sold over $40 million of UAL stock before UAL commenced its bankruptcy case.[32]

REASONS FOR DENYING THE PETITION

The petition for certiorari should be denied because it is procedurally defective, there is no intercircuit conflict, and the petition fails to satisfy any of the criteria specified by Supreme Court Rule 10 for issuance of a writ.

The petition is procedurally defective because it improperly requests the Court to affirm a lower court ruling on the responsibilities of directed trustees, and the argument that directed trustees and named fiduciaries have identical duties was never raised below and cannot be raised for the first time in a petition for certiorari.

Contrary to petitioner's claims, there is no intercircuit conflict as the Seventh Circuit's opinion in *Summers* is the only court of appeals to decide, based upon the evidence in the record, whether a directed trustee of an ESOP has a fiduciary duty to

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[29] R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 37), Ex. F (9/25/02 Fiduciary Committee Minutes).

[30] R.Doc.124 (SUF ¶ 22); R.Doc.130, Ex. 10 (Driscoll Decl., ¶ 38).

[31] R.Doc.124 (SUF ¶ 23); R.Doc.130, Ex. 1 (Declaration of Andrew Carron ("Carron Decl.")), Ex. A (Expert Report of Andrew Carron ("Carron Export Report"), ¶ 18).

[32] R.Doc.124 (SUF ¶ 24); R.Doc.130, App. 10 (Driscoll Decl., ¶ 38).

replace the employer's stock with another investment, and if so, what evidence would be sufficient to overcome the presumption that directed trustees of an ESOP fulfill their fiduciary duties by following the directions of the named fiduciaries to remain invested in employer stock.

To fabricate a conflict, Petitioners argue for the first time in these proceedings that directed trustees and named fiduciaries have identical fiduciary duties, that *Summers* concluded directed trustees and named fiduciaries have identical duties, and that a conflict exists as a result of the purported differences between *Summers* and the courts of appeals decisions determining whether and when *named fiduciaries* breach their fiduciary duties in failing to diversify an ESOP.

Petitioners' logic fails because they premise their argument on misstatements of law and the *Summers* holding. ERISA's statutory framework distinguishes the responsibilities of named fiduciaries and directed trustees, requiring directed trustees to follow the directions of the named fiduciaries and/or the plan as long as the directions are consistent with ERISA. *Summers* follows this law, noting that the key word in the statute is "directed." The named fiduciaries make the fiduciary decision to remain invested in employer stock. The directed trustee may override the decision of the named fiduciaries and the terms of the ESOP if the decision is imprudent. It does not make fiduciary decisions in the first instance. No court of appeals has held that directed trustees' fiduciary duties are identical to those of the named fiduciaries.

After misstating both the law and the *Summers* holding, Petitioners compare *Summers* with the four courts of appeals that have considered when a named fiduciary has a duty to diversify an ESOP's investment and argue that the Seventh Circuit did not follow these cases because it created a new per se rule that the presumption that the fiduciary acted reasonably cannot be overcome by evidence of a stock drop, evidence that the stock would certainly drop further, and evidence that the

company was spending large amounts of money (as Petitioners contend they presented). In fact, the Seventh Circuit's holding is consistent with the four court of appeals decisions and the Seventh Circuit did not create a per se rule, but rather held that Petitioners failed to present sufficient evidence of risk to overcome the presumption of prudence.

In dicta, the Seventh Circuit suggested that Petitioners could have overcome the presumption with evidence that at the time UAL formed the ESOP, the creators of the Plan (the settlors) reasonably could not have intended to place risk-averse employees into a plan that provided for only one investment alternative. The Seventh Circuit correctly noted that the Petitioners never explored what the settlors' intent may have been and whether the financial condition of UAL reached a point where it would have been appropriate to diversify the ESOP because of excessive risk beyond that which settlors reasonably intended. Petitioners argue that the Seventh Circuit's "formulation" of the risk standard improperly requires an ad hoc analysis of the risk borne by individual plan participants. Petitioners are wrong. Petitioners distort and misinterpret the Seventh Circuit's decision, as it only suggests consideration of wages and other benefits of all employees in the context of evaluating the risk of an ESOP, the settlor's intent, and whether Petitioners had overcome the presumption of prudence.

In sum, the petition should be denied because it is procedurally defective and because there is no intercircuit conflict concerning the fiduciary duty of directed trustees and what constitutes sufficient evidence to overcome the presumption that directed trustees act prudently when they follow the directions of the named fiduciary and remain invested in employer stock.

I. THERE IS NO INTERCIRCUIT CONFLICT REGARDING THE FIDUCIARY DUTY OF DIRECTED TRUSTEES

A. Petitioners' Argument Is Procedurally Defective

Mischaracterizing the Seventh Circuit's decision, Petitioners argue that *Summers* correctly held that directed trustees and named fiduciaries have identical duties. Petition at 22-23. Petitioners argue that this conflicts with a 1994 Eighth Circuit decision that this Court should overrule. Petitioners' argument is procedurally defective. Petitioners ask this Court to accept certiorari in order to affirm the Seventh Circuit's decision on the responsibilities of directed trustees, follow *FirsTier Bank, N.A. v. Zeller*, 16 F.3d 907 (8th Cir. 1994), and overrule *Maniace v. Commerce Bank, N.A.*, 40 F.3d 264 (8th Cir. 1994). Certiorari should not be granted to affirm a holding of the lower court.[33]

Moreover, Petitioners' argument that directed trustees and named fiduciaries have identical fiduciary duties was not raised below and cannot be raised for the first time in a petition for certiorari. *See Clingman v. Beaver*, 544 U.S. 581, 597-98 (2005).

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[33] Robert L. Stern et al., *Supreme Court Practice* ¶ 6.16 at 385 (8th Ed. 2002); *see also Lindheimer v. Illinois Bell Tel. Co.*, 292 U.S. 151, 176 (1934) ("The Company was successful in the District Court and has no right of appeal from the decree in its favor. The Company is not entitled to prosecute such an appeal for the purpose of procuring a review of the findings of the court below with respect to the value of the Company's property or the other findings of which it complains."); *Pub. Serv. Comm'n. v. Brashear Freight Lines, Inc.*, 306 U.S. 204, 206-207 (1939) (citations omitted) ("The Public Service Commission as the successful party below has no standing to appeal from the decree denying the injunction. And as no appeal has been taken to review the decree denying the injunction, this Court is without jurisdiction.").

B. The Seventh Circuit Held A Directed Trustee Has Limited Fiduciary Duties

The Seventh Circuit acknowledged State Street was a "'directed' trustee, [pursuant to 29 U.S.C. § 1103(a)(1)] because the Committee (the fiduciary named in the plan), in accordance with the plan language . . . , directed State Street to invest the ESOP's assets exclusively in stock of United Air Lines." *Summers*, 453 F.3d at 406. Title 29 U.S.C. § 1103(a)(1) specifically recognizes that trustees have limited authority or discretion when:

> the plan expressly provides that the trustee or trustees are subject to the direction of a named fiduciary who is not a trustee, in which case the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to [ERISA].

Recognizing § 1103(a)(1) limits the discretion of directed trustees, the Seventh Circuit first addressed whether this statutory provision eliminated a directed trustee's fiduciary duty entirely or merely limited it. The Seventh Circuit set forth the issue as follows: "We must first decide whether a directed trustee of an ESOP has *any* fiduciary duty with respect to the choice of trust assets, specifically any duty ever to replace the employer's stock — the normal holding of an ESOP — with some other security." *Summers*, 453 F.3d at 406 (emphasis added).

The Seventh Circuit held that a directed trustee is a fiduciary because the statute pertaining to directed trustees, § 1103(a)(1), specifies that the directed trustee cannot rely upon directions that are contrary to ERISA. Quoting § 1103(a)(1), the Seventh Circuit held: "the directed trustee 'shall be subject to *proper* directions of [the named] fiduciary which are made in accordance with the terms of the plan and w*hich are not contrary to [ERISA].*'" *Summers*, 453 F.3d at 406 (emphasis and alterations in original).

Focusing on the statutory language, the Seventh Circuit stated: "'[D]irect' is the critical word . . . the trustee can disobey the named fiduciary's directions when it is plain that they are imprudent." *Summers*, 453 F.3d at 406 (alteration in original). *Summers* held that the language of the statute makes clear that a directed trustee has no "'direct obligation to determine the prudence of a transaction' entrusted by the plan to another fiduciary." *Summers*, 453 F.3d at 406 (quoting U.S. Department of Labor Employee Benefits Security Administration, Fiduciary Responsibilities of Directed Trustees, Field Assistance Bulletin 2004-03 (Dec. 17, 2004) (the "DOL Bulletin") at 4). In arguing directed trustees and named fiduciaries have identical duties, and that *Summers* held the duties were identical, Petitioners fail to explain § 1103(a)(1).

In analyzing the question whether trustees have any fiduciary duties concerning the choice of trust assets, the Seventh Circuit noted a "split" of opinion between (a) those courts that have suggested that directed trustees *have no fiduciary duties* (citing *Herman v. NationsBank Trust Co.*, 126 F.3d 1354, 1361-62 (11th Cir. 1997) (noting in dicta that directed trustees do not have any fiduciary duties) and *Maniace*, 40 F.3d at 267-68 (finding that directed trustee did not have any fiduciary duty to diversify the plan assets because of specific language in the plan)), and (b) those courts that hold directed trustees are fiduciaries (citing *FirsTier*, 16 F.3d at 911 and *In re WorldCom, Inc. ERISA Litig.*, 354 F. Supp. 2d 423, 444-45, 449 (S.D.N.Y. 2005)). *Summers*, 453 F.3d at 406.

Petitioners mischaracterize the "split" mentioned by the Seventh Circuit to assist them in misconstruing the Seventh Circuit's holding. The Third and Eleventh Circuits have "stated their views" "in *dicta* in cases that did not involve directed trustees" (as Petitioners acknowledge at p. 24), indicating that directed trustees are not fiduciaries. *Herman*, 126 F.3d at 1361 (stating a directed trustee "is not subject to the fiduciary requirement in § 1104(a) to act prudently"); and *Moench v.*

Robertson, 62 F.3d 553, 571 (3d Cir. 1995). In *Maniace*, the Eighth Circuit held that the directed trustee was a fiduciary,[34] but that plaintiffs failed to demonstrate that the purchase of the employer's stock violated the plan or was contrary to ERISA. *Maniace*, 40 F.3d at 268. In reaching this conclusion, the court noted that the underlying fiduciary direction was not a violation of ERISA. *Id. See also Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090, 1103 (9th Cir. 2004) ("If the underlying fiduciary direction itself is not in violation of ERISA, the directed trustee's compliance with that direction cannot serve as a basis for liability.").

Petitioners argue that *FirstTier*, which the Seventh Circuit relied upon in concluding that directed trustees are fiduciaries, held that directed trustees are identical to named fiduciaries. Petitioners fail to discuss *WorldCom*, which the Seventh Circuit also relied upon in reaching its conclusion that directed trustees are fiduciaries. Neither *FirstTier* nor *WorldCom* held that directed trustees' fiduciary duties are identical to named fiduciaries.

WorldCom and *FirsTier* recognize that although "directed trustees" are fiduciaries, not all ERISA fiduciaries are the same, and the fiduciary duties of directed trustees are "'significantly narrower than the duties generally ascribed to a discretionary trustee under common trust principles.'" *WorldCom*, 354 F. Supp. 2d at 446 (quoting the DOL Bulletin at 2); *FirsTier*, 16 F.3d at 911 (finding that § 1103(a)(1) "modifies" the extent of a

[34] The opinion contains language stating that the directed trustee does not "fit within the ERISA definition of a fiduciary," and its conduct is governed exclusively by § 1103(a)(1). *Maniace*, 40 F.3d at 268. However, the Eighth Circuit also implicitly acknowledged the directed trustee was a fiduciary when it analyzed whether the directed trustee was liable as a co-fiduciary. *Id.* It concluded the directed trustee was not liable as a co-fiduciary because the named fiduciary had not breached its fiduciary duties and therefore plaintiffs could not show that the directed trustee either participated in said breaches or knew of the breaches and did nothing to remedy them. *Id.*

directed trustee's fiduciary duties). A directed trustee has no duty to render investment advice or "investigate the wisdom of [the named fiduciary's investment] choices or any obligation to render advice regarding the choices." *WorldCom*, 354 F. Supp. 2d at 449.

The Seventh Circuit's holding in *Summers* is consistent with other courts of appeals decisions and the position of the Department of Labor. *See Wright*, 360 F.3d at 1103 (discussion of trustee's limited liability under ERISA assumes a directed trustee is a fiduciary); *LaLonde v. Textron, Inc.*, 369 F.3d 1, 7 (1st Cir. 2004) (same); DOL Bulletin at 2 (directed trustees have "significantly narrower" fiduciary responsibilities designed to ensure that the directions it receives from the named fiduciary are in accordance with the plan and not contrary to ERISA).[35]

II. THE SEVENTH CIRCUIT DID NOT CREATE A NEW STANDARD

A. The Seventh Circuit Followed The Abuse Of Discretion Standard

Beginning with *Moench*, courts of appeals that have considered whether and when a fiduciary has a duty to diversify employer stock in an ESOP have uniformly held that a duty exists, but that the decision to remain invested in employer stock is limited to a review for an abuse of discretion. *Moench*, 62 F.3d at 571. *See, e.g., LaLonde*, 369 F.3d at 4; *Kuper v. Iovenko*, 66 F.3d 1447, 1459 (6th Cir. 1995); *cf. Wright*, 360 F.3d at 1097-98 (questioning whether any duty existed at all, but ultimately applying the abuse of discretion standard). Petitioners argue that the Seventh Circuit did not follow *Moench* and its progeny, but instead set forth a "new standard," thereby creating a split in

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[35] Courts grant "considerable and in some cases decisive weight" to interpretive bulletins depending on, among other things, the "thoroughness evident in its consideration, the validity of its reasoning, [and] its consistency with earlier and later pronouncements. . . ." *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944).

the circuits. Petition at 14. A brief explanation of the development of the standard illustrates why the Seventh Circuit's decision is consistent with the four other courts of appeals that have considered the issue.

Employee stock ownership plans like the Plan, are, in accordance with 29 U.S.C. § 1104(a)(2), exempt from ERISA's duty to diversify the investments of the plan "so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so. . . ." 29 U.S.C. § 1104(a)(1)(C). The Seventh Circuit held that § 1104(a)(2) and the language of a plan cannot "be interpreted to include a per se prohibition against diversifying an ESOP," because an ESOP fiduciary still has a duty of prudent investment that can override plan restrictions and § 1104(a)(2) in "special circumstances." *Summers*, 453 F.3d at 407 (quoting *Kuper*, 66 F.3d at 1457).

In developing the standard, the courts of appeals noted there are two competing concerns at issue: "Congress expressly intended that the ESOP would be both an employee retirement benefit plan and a 'technique of corporate finance' that would encourage employee ownership." *Martin v. Feilen*, 965 F.2d 660, 664 (8th Cir. 1992) (quoting 129 Cong. Rec. S16629, S16636 (Daily ed. Nov. 7, 1983) (statement of Sen. Long)). The courts of appeals attempted to find "a way for the competing concerns [of ERISA fiduciaries and ESOPs] to coexist." *Moench*, 62 F.3d at 570. Normally fiduciaries' investment decisions are subject to a strict standard of review, but such scrutiny in the context of an ESOP "would render meaningless the ERISA provision excepting ESOPs from the duty to diversify." *Id.*

The courts of appeals therefore apply a deferential standard to the fiduciary's decision not to diversify assets of an ESOP: a fiduciary's decision to remain invested in employer stock is presumed to be proper and that presumption can only be overcome by showing an "abuse of discretion." *Moench*, 62 F.3d at 571. "In attempting to rebut the presumption, the plaintiff

may introduce evidence that 'owing to circumstances not known to the settlor and not anticipated by him [the making of such investment] would defeat or substantially impair the accomplishment of the purposes of the trust.'" *Id.* (alteration in original) (quoting *Restatement (Second) of Trusts* § 227 cmt. g (1957)).

The Seventh Circuit set forth the standard it intended to follow to review the alleged failure to diversify the Plan. Fiduciaries may be required to:

> begin diversifying the ESOP's assets at the point at which an increase in the riskiness of the assets, had it been foreseen, would have induced the creators of the ESOP either to have not created it at all or to have required at least partial diversification. (. . . .) **Or,** as *Kuper v. Iovenko*, *supra*, 66 F.3d at 1459, puts it, "the plaintiff must show that the ERISA fiduciary could not have reasonably believed that the plan's drafters would have intended under the circumstances that he continue to comply with the ESOP's direction that he invest exclusively in employer securities." *See also Moench v. Robertson*, 62 F.3d 553, 571-72 (3d Cir. 1995).

Summers, 453 F.3d at 410 (emphasis added).

By first setting forth its articulation of the standard it intended to apply, and then using the word "or" and quoting the standard from *Kuper* and *Moench*, the Seventh Circuit did not intend to announce a "new" standard. *Summers* did not criticize *Moench* or its progeny, or otherwise state that it would deviate from the standard set forth in *Moench*. Significantly, the Seventh Circuit did not state that it was creating a split in the courts of appeals by rendering its decision. If the Seventh Circuit intended to create, or believed its decision created, an intercircuit conflict, it was obligated to circulate its opinion sua sponte to the full court in advance of publication pursuant to Seventh Circuit Rule

40(e), which it did not do. *See, e.g., United States v. Mitchell*, 353 F.3d 552, 561 n.9 (7th Cir. 2003) ("Because this opinion will create a conflict among the Circuit Courts, it has been circulated to all of the judges of this court in regular active service pursuant to Circuit Rule 40(e).").

1. The Seventh Circuit Concluded Petitioners' Evidence Did Not Overcome The Presumption That The Continued Investment In Employer Stock Was Prudent

The Seventh Circuit affirmed the grant of summary judgment in State Street's favor because of Petitioners' "failure of proof." *Summers*, 453 F.3d at 411. Petitioners "made no effort" to establish the point at which the ESOP trustee should sell in order to protect the employee-shareholders against "excessive risk." *Id.* Petitioners cobble together a circuit "conflict" based not on any difference in the legal standard, but rather on the application of a contextually-based test that leads to different results depending on the underlying factual circumstances and the evidence in the record. *See* Petition at 15-16 (agreeing with the Seventh Circuit's statement of the rule or the court's "basic concept," but criticizing the "formulation" or application of the standard). This Court should not grant "certiorari to review evidence and discuss specific facts." *United States v. Johnston*, 268 U.S. 220, 227 (1925). *See also NLRB v. Hendricks County Rural Elec. Membership Corp.*, 454 U.S. 170, 176 n.8 (1981) (finding improvident grant of cross-petition that presented "primarily . . . a question of fact, which does not merit Court review"); Sup. Ct. R. 10 (noting the Court will "rarely" grant review where lower court has arguably misapplied "a properly stated rule of law").

Petitioners argued that the Goodwin Letter and the drop in UAL's stock price shortly thereafter demonstrated UAL's impending collapse, thus requiring diversification of the Plan. They also argued that State Street should have started selling the UAL stock within 30 days after the issuance of the Goodwin

Letter. The Seventh Circuit found that the evidence did not support Petitioners' erroneous factual conclusion, i.e., the drop in the stock price did not reflect UAL's impending collapse. As the Seventh Circuit noted:

> The plaintiffs say the letter should have alerted State Street that United was going into the tank. That is wrong. After the market "read" the letter, it valued United stock at $15.05 a share. Had the market thought that United would be bankrupt by the end of 2002, it would not have priced its stock that high in October 2001, implying a market capitalization for the company of more than $800 million.

Summers, 453 F.3d at 408. The Seventh Circuit found that it was not imprudent for State Street to assume that a major stock market "provides the best estimate of the value of the stocks traded on it," and it was not "required to act on the assumption that the market was overvaluing United." *Id.* Moreover, the argument that State Street "should have outsmarted the market...is not a correct interpretation of the duty of prudent management of trust funds. . . ." *Id.* at 412.

2. *Summers* Did Not Create A Conflict In Its Application Of The Legal Standard

The cases Petitioners cite do not conflict regarding the application of the "abuse of discretion" standard to the underlying facts. First, *Summers* involved the application of the abuse of discretion standard to the decision of a directed trustee not to override the decision of the named fiduciary to remain invested in employer stock. Only one case upon which Petitioners rely applied the *Moench* standard to directed trustees, and Petitioners do not rely upon or reference that portion of the decision — nor could they. The application of the abuse of discretion standard in *LaLonde* to the actions of the directed trustee are consistent with the Seventh Circuit's *Summers* decision. As noted above, in *LaLonde*, the First Circuit held

that the plaintiffs failed to state a claim against the directed trustee because the allegations were only that the directed trustee knew the company's stock price and profits were declining and that the company was undergoing a restructuring. *LaLonde*, 369 F.3d at 6-7.

Second, there are no guidelines specifying what is and what is not an abuse of discretion. In applying the abuse of discretion test, no court of appeals has ever held that an ESOP fiduciary abused its discretion by failing to diversify the plan assets, and only one other court of appeals has had the opportunity to consider whether the evidence presented was sufficient to state a claim. *See generally*, *Kuper*, 66 F.3d 1447.

Courts of appeals have, in dicta, suggested factual scenarios that might be sufficient to trigger a duty to diversify. For example some courts have suggested that evidence of a company's impending collapse would be sufficient. *Moench*, 62 F.3d at 572. Other courts have suggested that there may be situations where defendant fiduciaries have knowledge of some impropriety such as misrepresentation, fraud or accounting irregularities and that these situations in combination with the financial condition of the company might trigger a duty to diversify. *See*, *e.g.*, *WorldCom*, 354 F. Supp. 2d at 449-50 (accounting fraud); *In re Sprint Corp. ERISA Litig.*, 388 F. Supp. 2d 1207, 1223-24 (D. Kan. 2004) (misrepresentation). In *Steinman v. Hicks*, the Seventh Circuit noted the following factual scenario might trigger the duty:

> [If the] ESOP was [the employees'] principal retirement asset . . . and was entirely invested in the stock of their employer . . . , and their employer was bought in a stock-for-stock deal—so that all the assets of the ESOP became stock in the acquirer—by a company that had a much higher debt-equity ratio than their (former) employer and as a result its stock price was much more volatile and its bankruptcy risk greater. Then, even if the trustees

> did not predict the company's "impending collapse," they might be required in the interest of the participants either to diversify the plan's stockholdings or to exchange the . . . stock for Treasury bills.

352 F.3d 1101, 1106 (7th Cir. 2003).

Other than *Summers*, *Kuper* is the only one of the cases cited by Petitioners that decided the merits of a district court's judgment for the defendants. *Kuper*, 66 F.3d 1447. *Kuper* affirmed the district court's trial judgment, noting that while plaintiffs presented evidence that the employer stock was declining and defendants were aware of events that would continue to cause the stock to decline in value, defendants presented evidence that the stock fluctuated and several investment advisors recommended holding the stock. *Id.* at 1460. *Kuper*'s holding is consistent with *Summers*.

3. The Seventh Circuit Did Not Create A Per Se Rule

Petitioners argue that the Seventh Circuit announced a new per se rule that evidence that stock "plummet[ed]," "the underlying company" continued to "hemorrhage money," and the company failed to address the problems causing the decline in the stock price were insufficient to overcome the presumption of prudence. Petition at 14. Petitioners do not quote or point to any language in the Seventh Circuit's decision that could support this claim of a new "rule."

The Seventh Circuit did not conclude that the evidence Petitioners presented demonstrated that the stock was "plummeting," would continue to plummet, that the company was "hemorrhaging money," and that UAL was not addressing problems that were causing a decline in its stock price.

In addition, Petitioners' argument that the Seventh Circuit's new per se rule excluded consideration of "the intentions of the

Plan's settlor" is incorrect. Petition at 15. The Seventh Circuit noted that the *Moench* presumption could be overcome by evidence that the increase in the riskiness of the assets, "had it been foreseen, would have induced the *creators of the ESOP [the settlors]* either to have not created it at all or to have required at least partial diversification." *Summers*, 453 F.3d at 410 (emphasis added). Petitioners did not present any evidence of the settlor's intent, nor do they point to such evidence in the record.

B. The Seventh Circuit's Examples Of Excessive Risk Did Not Create A New Rule

To determine what constitutes excessive risk sufficient to require an ESOP fiduciary to override the terms of the plan to fulfill its duty of prudence, the Seventh Circuit contemplated possible approaches a court may utilize depending on the facts and circumstances of each case. For example, in *Steinman*, in dicta, the Seventh Circuit considered how to evaluate the impact of a merger on an ESOP, concluding that it may be appropriate to evaluate the merged company's debt-to-equity ratio and the nature and character of the post-merger stock. *Steinman*, 352 F.3d at 1106. Applying basic economic principles, the court noted that the ESOP now held stock whose price was more volatile and the company's risk of bankruptcy was greater, thereby increasing the risk of the ESOP. *Id.*

Turning to *Summers*, the Seventh Circuit suggested possible criteria to consider in a stock drop case to evaluate the risk of investing in company stock in a market where the stock is declining, including benefits received by employees in the form of income derived from continued employment and other fringe benefits.[36] Because Petitioners did not explore these issues or demonstrate facts sufficient to show excessive risk during the

[36] The evidence in this case showed United provided participants with a diversified 401(k) plan and a defined benefit plan. *See* R.Doc.129, Committee Def. Ex. 5 (Deposition of Craig Musa ("Musa Depo"), 20:09-23:02).

relevant time period, the Seventh Circuit found there was a failure of proof.

Petitioners misstate that the Seventh Circuit created a new fiduciary liability standard requiring the court to the consider the individual assets of each participant and the projected wealth of the employees/participants outside of the ESOP. Petitioners confuse the analysis of the settlor's intent and whether the settlor would have established an undiversified plan in light of conditions reflecting excessive risk to the employees/participants (and which may include an evaluation of the assets of employees outside the plan, including wages, other plans, and fringe benefits) with the analysis of fiduciary liability (which focuses on whether the fiduciaries were acting in the best interests of the plan as a whole and precludes a fiduciary from being partial to any one group of beneficiaries). Under *Kuper*, to determine whether to disregard the terms of the plan, the plaintiff must examine the settlor's intent and show that the ERISA fiduciary could not have reasonably believed that the plan's drafters would have intended under the circumstances that he continue to comply with the ESOPs direction to invest exclusively in employer securities. *Kuper*, 66 F.3d at 1459. This evaluation may include consideration of the wages and benefits of UAL's employees outside of the plan. *See Summers v. State Street Bank & Trust Co.*, 104 F.3d 105, 107-109 (7th Cir. 1997) (the settlors of the UAL ESOP intended to create a retirement plan that would get voting control of the company and majority equity ownership in exchange for accepting lower wages and fringe benefits for a substantial period).

C. The Existence Of Pending Litigation In The Lower Courts Involving "These Issues" Does Not Require This Court To Grant The Petition

Petitioners claim that there is "massive ongoing litigation in the lower courts," involving the "issues" raised in the petition, requiring this Court to accept the petition to provide a "uniform standard" to guide the lower court's decisions. Petition at

21-22. Petitioners cite fourteen district court cases decided in 2006 and a law review article discussing approximately fifty court decisions.

Petitioners do not argue that these decisions create a conflict requiring this Court to grant certiorari, or identify any other reason these cases require review under Rule 10. The majority of the cases Petitioners reference are district court decisions. Petitioners fail to explain why cases pending in the district courts warrant this Court's review of *Summers*. Furthermore, not all of the cases Petitioners reference are currently "pending." *See, e.g., Rankin v. Rots*, No. 02-CV-71045, 2006 U.S. Dist. LEXIS 45706 (E.D. Mich. June 28, 2006) (approval of settlement); *In re IKON Office Solutions Sec. Litig.*, 209 F.R.D. 94 (E.D. Pa. 2002) (same)); *In re WorldCom Inc. ERISA Litig.*, No. 02 Civ. 4816, 2004 U.S. Dist. LEXIS 20671 (S.D.N.Y. Oct. 18, 2004) (same).

Nor do Petitioners identify the "issues" these cases decided that are allegedly raised in the petition. Many of the cases involve issues that are not relevant here. For example, some of the cases involved class certification issues. *See, e.g., In re Aquila ERISA Litig.*, 237 F.R.D. 202 (W.D. Mo. 2006); *In re Elec. Data Sys. Corp. "ERISA" Litig.*, 224 F.R.D. 613 (E.D. Tex. 2004); *In re Qwest Sav. & Inv. Plan ERISA Litig.*, No. 02-RB-464, 2004 U.S. Dist. LEXIS 24693 (D. Colo. Sept. 27, 2004). Other decisions involved approvals of settlement. *See, e.g., Rankin v. Rots*, No. 02-CV-71045, 2006 U.S. Dist. LEXIS 45706 (E.D. Mich. June 28, 2006) (approval of settlement); *In re IKON Office Solutions Sec. Litig.*, 209 F.R.D. 94 (E.D. Pa. 2002) (same); *In re WorldCom Inc. ERISA Litig.*, No. 02 Civ. 4816, 2004 U.S. Dist. LEXIS 20671 (S.D.N.Y. Oct. 18, 2004) (same).

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX A — 29 U.S.C.S. § 1002(21)(A)

§ 1002. Definitions

For purposes of this title:

. . . .

(21) (A) Except as otherwise provided in subparagraph (B), a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designated under section 405(c)(1)(B) [29 USCS § 1105(c)(1)(B)].

. . . .

APPENDIX B — 29 U.S.C.S. § 1102(a)(2)

§ 1102. Establishment of plan

(a) Named fiduciaries.

(1) Every employee benefit plan shall be established and maintained pursuant to a written instrument. Such instrument shall provide for one or more named fiduciaries who jointly or severally shall have authority to control and manage the operation and administration of the plan.

(2) For purposes of this title, the term "named fiduciary" means a fiduciary who is named in the plan instrument, or who, pursuant to a procedure specified in the plan, is identified as a fiduciary (A) by a person who is an employer or employee organization with respect to the plan or (B) by such an employer and such an employee organization acting jointly.

. . . .

APPENDIX C — FEDERAL RULE OF CIVIL PROCEDURE 56(c)

Rule 56. Summary Judgment

. . . .

Motion and Proceedings Thereon. (c) The motion shall be served at least 10 days before the time fixed for the hearing. The adverse party prior to the day of hearing may serve opposing affidavits. The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. A summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages.

. . . .

APPENDIX D — SEVENTH CIRCUIT RULE 40(e)

Circuit Rule 40. Petitions for Rehearing

. . . .

(e) *Rehearing Sua Sponte Before Decision.* A proposed opinion approved by a panel of this court adopting a position which would overrule a prior decision of this court or create a conflict between or among circuits shall not be published unless it is first circulated among the active members of this court and a majority of them do not vote to rehear en banc the issue of whether the position should be adopted. In the discretion of the panel, a proposed opinion which would establish a new rule or procedure may be similarly circulated before it is issued. When the position is adopted by the panel after compliance with this procedure, the opinion, when published, shall contain a footnote worded, depending on the circumstances, in substance as follows:

> This opinion has been circulated among all judges of this court in regular active service. (No judge favored, or, A majority did not favor) a rehearing en banc on the question of (e.g., overruling *Doe v. Roe*.)

(2)

No. 06-439

IN THE

Supreme Court of the United States

JERRY SUMMERS, GEORGE T. LENORMAND, JEFFERY D. CRITES, LOUISE VAN RENSBURG and JAMES E. SHAMBO, individually and on behalf of all others similarly situated,

Petitioners,

v.

STATE STREET BANK & TRUST COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY BRIEF

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INTRODUCTION

The central legal issue in *dozens* of currently-pending cases is the question of when the fiduciaries of employee stock ownership plans ("ESOPs") have a duty to reduce plan holdings of employer stock pursuant to the Employee Retirement Income Act of 1974 ("ERISA"), 29 U.S.C. §§ 1001 *et seq.* *See* Petition at 21-22 (collecting cases). The Courts of Appeals are divided on the question, although most have followed *Moench v. Robertson*, 62 F.3d 553, 571-72 (3d Cir. 1995), which holds that "the plaintiff may overcome that presumption [that an ESOP fiduciary who invests the assets in employer stock acted consistently with ERISA] by establishing that the fiduciary abused his discretion by investing in employer securities."

In the instant case, however, the Seventh Circuit added greatly to the confusion surrounding the duties of ESOP fiduciaries by becoming the first court to hold that there can never be a duty to sell company stock unless (i) the stock does not trade in an "efficient market" and (ii) the fiduciary has conducted a participant-by-participant analysis and determined that the ESOP participants' other sources of income or retirement savings are not sufficient to warrant the absorption of increased risk in the ESOP investment. *Summers v. State Street Bank & Trust Co.*, 453 F.3d 404, 409-411 (7th Cir. 2006). Not only is the Seventh Circuit's standard a radical departure from the *Moench* standard, but, as the Seventh Circuit admits, its standard "may be beyond the practical capacity of the courts" to apply. *Id.* at 411. Surely Congress could not have intended such a result in a statute that is widely recognized to impose the "highest [obligations] known to law" on fiduciaries.[1]

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1. *See, e.g.*, *Donovan v. Bierwirth*, 680 F.2d 263, 272 (2d Cir. 1982) (Friendly, J.); *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 294 (5th Cir. 2000); *Chao v. Hall Holding Co.*, 285 F.3d 415, 426 (6th Cir. 2002); *Howard v. Shay*, 100 F.3d 1484, 1488 (9th Cir. 1996); *ITPE Pension Fund v. Hall*, 334 F.3d 1011, 1013 (11th Cir. 2003).

In its effort to evade this Court's review, State Street erroneously asserts that "the petition is procedurally defective because it improperly requests the Court to affirm a lower court ruling. . . ." Resp. Br. at 9. To the contrary, Petitioners ask this Court to ***reverse*** the lower courts' grant of summary judgment in State Street's favor. Indeed, under the appropriate standard (which would ***not*** consider ESOP participants' non-plan assets), Plaintiffs/Petitioners are entitled to a trial on the question of whether State Street was obliged to act ***before*** the stock became virtually worthless.[2]

Next, State Street contends that this Court should not consider upholding the Seventh Circuit's ruling that "directed trustees" have the same co-fiduciary and fiduciary duties as other fiduciaries since the argument "was not raised below." Resp. Br. at 12-13. State Street's contention makes no sense: the Seventh Circuit's ruling is reviewable by this Court regardless of whether Petitioners raised the issue. In any event, Petitioners ***did*** argue below that (i) State Street, as the ESOP's trustee, was a fiduciary subject to the duties of prudence and loyalty pursuant to 29 U.S.C. § 1104(a); and (ii) State Street was also subject to the same co-fiduciary duties of loyalty as all other fiduciaries pursuant to 29 U.S.C. § 1105(a)(3).[3]

Finally, State Street contends that that Seventh Circuit's decision in *Summers* should not be reviewed because it "is consistent with . . . the position of the Department of Labor" ("DOL") that there can be no duty to sell until bankruptcy is a certainty. Resp. Br. at 17. To the contrary, the *Summers* court

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2. Only at that time, in the late summer of 2002, did State Street ***finally*** confront the ESOP Committee with its patent and ongoing breach of fiduciary duty – at which point State Street was almost ***immediately*** appointed as investment manager with the explicit power to begin diversifying the ESOP's holdings of UAL stock. *See* R. Doc.# 178, Plfs' Add'l Facts, ¶¶ 156, 167 and R.Doc.# 184, Plfs. Ex. 25 at UAL-SUM 00047, 00080.

3. *See, e.g.*, Plaintiffs-Appellants', Cross-Appellees' Brief and Short Appendix in Case No. 05-4005 (Seventh Circuit) at 26.

explicitly ***rejected*** the DOL's new position, finding that the DOL's standard "is not an administrable" one, and that "selling when bankruptcy is declared will almost certainly be too late." 453 F.3d at 411.

In short, the Seventh Circuit's decision in this case (i) creates a Circuit split as to the duties of ESOP fiduciaries and (ii) adds to the Circuit split as to the duties of so-called "directed trustees." Both issues are in need of resolution by this Court.

ARGUMENT

A. The Seventh Circuit's New Standard Creates A Conflict Concerning The Obligations Of ESOP Fiduciaries When The Company Is Collapsing

Prior to this case, the Courts of Appeals were generally in agreement that, depending upon the surrounding circumstances of the company whose stock is at issue, ESOP fiduciaries can have a duty to begin diversifying the plan's company stock holdings. *See, e.g., Moench v. Robertson*, 62 F.3d 553, 571-72 (3d Cir. 1995); *accord LaLonde v. Textron, Inc.*, 369 F.3d 1, 4, 6 (1st Cir. 2004); *Kuper v. Iovenko*, 66 F.3d 1447, 1458-59 (6th Cir. 1995); *but see Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090 (9th Cir. 2004) (questioning whether there can ever be any such duty, but applying *Moench* to the case before it).

Here, while paying lip service to *Moench*, the Seventh Circuit ***in fact*** crafted a new standard; this standard is ***not*** based on ERISA and the cases construing it, but instead purports to be based on sources such as *The Modern Theory of Corporate Finance*[4] and *Principles of Economics*.[5] *See Summers*, 453 F.3d at 409. Whatever intellectual interest these sources may excite, they are nowhere embodied in the text of ERISA.

According to the *Summers* court, ***any*** argument that ESOP fiduciaries have a duty to sell based (as here) on the extraordinary

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4. Clifford W. Smith, Jr., ed. (2d Edition 1990).

5. N. Gregory Mankiw (1998).

and public collapse of a company ***must*** fail by virtue of a novel application of the "efficient market" theory: "at ***every*** point in the long slide of United's stock price, that price was the best estimate available either to State Street or to the Committee of the company's value, . . . so neither fiduciary was required to act on the assumption that the market was overvaluing United." *Summers*, 453 F.3d at 408 (emphasis in original). This *per se* "market-price" rule (that there can never be any duty to sell a publicly-traded stock where the market is efficient) stands in contrast to the *Moench* standard under which an ESOP plaintiff can prevail "by showing that a prudent fiduciary acting under similar circumstances would have made a different investment decision." *See Kuper*, 66 F.3d at 1459. The requirement to consider the surrounding circumstances, in turn, comes directly from the language of ERISA itself, which requires that ***all*** fiduciaries exercise "the care, skill, prudence, and diligence under the circumstances then prevailing." 29 U.S.C. § 1104(a)(1)(B).[6] Thus, the Seventh Circuit's *per se* "market price" rule finds no support in the statute, either.

Perhaps even more radically, the *Summers* court holds that a plan participant can ***never*** prevail in an ERISA "company stock" case ***unless*** he can prove he lacked substantial ***non-plan*** assets. *See* Pet. at 16-17. As the *Summers* court puts it, ERISA's prudence requirement ***can*** require the diversification of ESOP assets when the "risk" of company stock becomes "excessive" within the context of the participant's portfolio: "How excessive would depend in the first instance on the amount and character of the employees' other assets, for, as we have already indicated, it is the riskiness of one's portfolio, not of a particular asset in the portfolio, that is important to the risk-averse investor." *Summers*, 453 F.3d at 411.

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6. While State Street is correct that ESOP fiduciaries are, of necessity, not subject to the *per se* diversification requirement that applies to other ERISA plan investments, there is also no dispute that ESOP fiduciaries remain subject to the same duty of prudence under the circumstances that applies to all ERISA fiduciaries.

State Street knows that the requirement that non-plan assets be considered is both new and indefensible, as evidenced by its response; according to State Street, the Seventh Circuit somehow did not mean what it said in this portion of its opinion. SS Opp. at 27. Plaintiffs respectfully submit that this portion of the opinion cannot be expunged, and, indeed, is the reason why the Seventh Circuit affirmed summary judgment against them here. *See Summers*, 453 F.3d at 411 (judgment affirmed because "[t]he plaintiffs never sought to explore these issues" of how much wealth the plan participants had outside of the ESOP; hence, "there has . . . been a failure of proof.")

The Seventh Circuit's opinion in *Summers* has plainly created a split amongst the circuits with respect to the duty of ESOP fiduciaries.

B. Petitioners Properly Seek Reversal Of The Seventh Circuit's Decision

Respondent mistakenly suggests that the petition is "procedurally defective" since Petitioners seek "to affirm a holding of the lower court." SS Opp. at 12. To the contrary, Petitioners *lost* in the Seventh Circuit, and seek review of that decision upholding the district court's grant of summary judgment in favor of State Street. This is simply ***not*** a case like those cited by Respondent in which the litigant "was successful in the [court below] and has no right of appeal from the decree in its favor." SS Opp. at 12 (quoting *Pub. Sev. Comm'n v. Brashear Freight Lines, Inc.*, 306 U.S. 204, 206-07 (1939)).

Nonetheless, Petitioners acknowledge that the *Summers* court favorably resolved one issue upon which the Courts of Appeals differ. Namely, the Seventh Circuit sided with those courts that have held that so-called "directed trustees" are nonetheless subject to ERISA's fiduciary and co-fiduciary duties. In order to set forth the proper standard governing ESOP fiduciaries in this case, this Court will necessarily reach the same question. Unfortunately for Petitioners, however, that fact does *not* convert Petitioners into the "prevailing parties" in the

court below. It also does not render their petition "procedurally defective."

C. The Circuit Courts Are Split As To The Existence And Scope Of The Fiduciary Obligations Of Directed Trustees

In this case, Petitioners bring claims against State Street for breaches of the duties of prudence and loyalty under 29 U.S.C. § 1104(a), and co-fiduciary breaches under 29 U.S.C. § 1105(a). Though State Street claims that Petitioners never argued that "directed trustees" have the same fiduciary duties as other ERISA fiduciaries, SS Opp. at 12-13, Petitioners ***in fact*** stressed that argument. As Petitioners noted in the Seventh Circuit: "While State Street focused its defense on the assertion that it was a mere 'directed trustee' within the meaning of 29 U.S.C. § 1103(a)(1), the 'directed trustee' defense is no defense to Plaintiffs' claim for breach of co-fiduciary duty." *See, e.g, FirsTier Bank, N.A. v. Zeller*, 16 F.3d 907, 911 (8th Cir. 1994) (directed trustee "is not relieved of its fiduciary duties . . . to attempt to remedy known breaches of duty by other fiduciaries . . ."). Plaintiffs-Appellants', Cross-Appellees' Brief at 26. *See id.* at 33 (directed trustee has duty "to conform to the prudent man standard of care"). These arguments echoed the arguments made by Petitioners in the trial court.

Moreover, this Court cannot credit State Street's argument that the Circuit Courts are ***not*** divided as to the fiduciary obligations of directed trustees. The statute on its face suggests that the "named fiduciary" is responsible for making decisions in the first instance, yet makes clear that directed trustees are ***not*** to follow directions that are "contrary to ERISA." 29 U.S.C. § 1103(a)(1). Notwithstanding this language, some courts have held that "directed trustees" have ***no*** fiduciary duties whatsoever. *See Maniace v. Commerce Bank, N.A.*, 40 F.3d 264, 267 (8th Cir. 1994); *Herman v. NationsBank Trust Co.*, 126 F.3d 1354, 1361-62 (11th Cir. 1997). The Seventh Circuit here voiced its agreement with *FirsTier Bank, N.A. v. Zeller*, 16 F.3d at 911,

and squarely held that "[l]ike other ERISA trustees, a directed trustee has a statutory duty of prudence. § 1104(a)(1)(B)." *Summers*, 453 F.3d at 406.

Try though it might, State Street can not whitewash this very real split amongst the Courts of Appeals. Likewise, State Street cannot mask the importance of that split, which is well-illustrated by this case. Here, as is not unusual, the so-called "named fiduciaries" (the ESOP Committee members) were employees and pilots at UAL with no particular background in either finance or ERISA. State Street, the industry professional, attended each and every Committee meeting. Hence, State Street was well-aware that – even after the extraordinary and devastating events of 9/11, even after the unprecedented remarks by the C.E.O. that accurately reported that the Company was "hemorrhaging money," and was "in a struggle just to survive," and even as the financial community recognized a significant and short-term risk of bankruptcy – the Committee ***never even discussed*** the problems at the Company, the tanking stock price, or the implications for the billion-dollar ESOP over which the Committee ostensibly presided.[7] At the same time, albeit unknown to the Committee, State Street was well-aware of the burgeoning crisis at UAL and was monitoring the stock as an "at risk" position.[8] Yet, no doubt planning to hide behind its "directed trustee" status, State Street chose not to act until the stock was nearly worthless. Only then, in the late summer of 2002, did State Street choose to act – when it did so, and informed the Committee Members of their fiduciary obligations, State Street was ***almost immediately*** appointed investment manager for the ESOP.[9] In this capacity, State Street belatedly began selling off Company stock – far too little and far too late for the hapless ESOP participants, who lost some $500 million dollars as a result of State Street's dilatoriness. Stunningly in

7. *See* Petition at 4-10.

8. *See id.* at 9-10.

9. *See id.* at 10-11.

light of its holding, the *Summers* court concludes, "what State Street may well have done wrong was to delay selling its United stock until too late to spare the employee-shareholders from bearing inordinate risk." *Summers*, 453 F.3d at 411. Under the appropriate standard of prudence under the circumstances, Petitioners submit, they are entitled to a trial on precisely that question.

Hence, the split amongst the Courts of Appeals as to the fiduciary duties of directed trustees is one with very real consequences in a large number of currently pending cases.[10] The resolution of the conflict will provide much needed-guidance for the courts and for trustees, and may provide protection for ERISA plan participants.

D. The Department of Labor's Latest Pronouncement Has Exacerbated The Confusion Amongst the Lower Courts

State Street incorrectly asserts that "The Seventh Circuit's holding in *Summers* is consistent with . . . the position of the Department of Labor" in its 2004 Field Assistance Bulletin concerning the fiduciary responsibility of directed trustees with respect to ESOP investments. SS Opp. at 17 (discussing U.S. Dept. of Labor, Field Assistance Bulletin No. 2004-03 (December 17, 2004)) ("FAB"). To the contrary, the *Summers* court flatly rejected the FAB standard as "not administrable." *Summers*, 453 F.3d at 411.

Yet the FAB standard has become highly influential. Indeed, a growing number of courts purport to follow the FAB's statement that directed trustees have a duty to question the holding of company stock in an ESOP only "in limited, extraordinary circumstances, where there are clear and compelling public indicators . . . that call into serious question a company's viability as a going concern." FAB at 5-6. Those

10. Once again, State Street cannot change this indisputable fact by pointing to a small number of cases that have settled, or not yet reached the essential issue as to the duties of directed trustees. *See* SS Opp. at 28-29.

courts – including the district court in this case – view the FAB as conveying almost total immunity for directed trustees. *See, e.g., Summers v. UAL Corporation ESOP Comm.*, No. 03 C 1537, 2005 U.S. Dist. Lexis 23918, at *13-15 (N.D. Ill. October 12, 2005) (quoting the FAB as quoted in *In re WorldCom, Inc. ERISA Litigation*, 354 F. Supp. 2d 423, 445-48 (S.D.N.Y. 2005)); *see also DiFelice v. U.S. Airways, Inc.*, 397 F. Supp. 2d 735, 751-52 (E.D. Va. 2005) (citing the FAB and holding that there can be no duty to sell company stock until the company files for bankruptcy); *In Re RCN Litig.*, 2006 U.S. Dist. Lexis 12929, at *13-16 (D.N.J. Mar. 21, 2006).

In setting forth the correct standard governing the conduct of directed trustees of ESOPs, this Court can consider whether the DOL's latest statement is entitled to any deference whatsoever.

In fact, the FAB is a radical departure from a series of broad pronouncements made by the DOL over the years concerning the scope of the fiduciary duties of a "directed trustee." According to one such pronouncement, a directed trustee "has a responsibility to exercise discretion where the directed trustee has reason to believe that the named fiduciary's directions are not made in accordance with the terms of the plan or are contrary to ERISA. . . ." *In re Enron Corp. Sec. Derivative & ERISA Litig.*, 284 F. Supp. 2d 511, 593 (S.D. Tex. 2003) (quoting DOL Opinion No. 92-23A). According to another, "even with regard to directions involving stock that has been allocated to an individual participant's account, the Department has taken the position that the trustee(s) remain(s) responsible for determining whether a violation of ERISA would occur if the participant's directions were followed." *In re Enron*, 284 F. Supp. 2d at 593 (quoting DOL Opinion of Aug. 19, 1994). In the *Enron* litigation, the DOL filed an *amicus* brief, stating that: "even if Northern Trust [as a directed trustee] had no discretionary role under the Savings Plan, as it asserts, it could not follow directions that it knew ***or should have known*** were imprudent

or disloyal in violation of ERISA §§ 404(a)(1)(A) and (B), 29 U.S.C. §§ 1104(a)(1)(A) and (B)" (emphasis added).[11]

Plaintiffs submit that this Court should withhold deference to the FAB given that the DOL has radically changed its position without explanation. *See, e.g., Good Samaritan Hosp. v. Shalala*, 508 U.S. 402, 417 (1993); *Norfolk S. Ry. v. Shanklin*, 529 U.S. 344, 356 (2000). The DOL has made no attempt to explain its departure from its prior liberal reading of the duties of directed trustee in favor of the extremely narrow view of the new FAB. In the absence of any explanation, Plaintiffs submit that the FAB is entitled to no deference. *Atchison, T. & S. F. R. Co. v. Wichita Bd. of Trade*, 412 U.S. 800, 808 (1973). In any event, the question of whether the FAB standard should in fact trump the opinions of the Courts of Appeals is ripe for resolution by this Court in this case.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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11. A copy of the brief is available at *http://www.dol.gov/sol/media/briefs/enronbrief-8-30-02.pdf*